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IN THE

Supreme Court of the United States

October Term, 1948

No. 511

IN THE MATTER OF

THE PEORIA AND EASTERN RAILWAY COMPANY

INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY,

Petitioners,

v.

THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

The Income Bondholders of The Peoria and Eastern Railway Company, petitioners, respectfully pray that a writ of certiorari issue to the United States District Court for the Southern District of New York, to review the final decree of that court, sitting as a three-judge Special Court, which decree was entered on November 16, 1948 (R. 39 or

S. 1),* in the Railroad Adjustment Proceeding, entitled In the Matter of The Peoria and Eastern Railway Company. Section 745 of the Bankruptcy Act, *infra*, p. 72, provides for such direct review in this Court. See p. 19, *infra*.

Opinions Below

The opinion of the Special District Court appears at R. 33 or S. 11, and its opinion on rehearing at R. 35 or S. 69. Both opinions are reported at 78 F. Supp. 312. The opinion in connection with the final decree appears at R. 38 or S. 77, and is not yet reported.**

The Report of the Special Master appears at R. 28 or S. M. 1. It is not reported.

Statutes Involved

The provisions of Chapter XV of the Bankruptcy Act are printed in the Appendix to this petition, *infra*, pp. 57-73.

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* Petitioners are moving to dispense with printing the large record in connection with the consideration of this petition for certiorari. The portions of the record deemed necessary to such consideration, with appropriate record references, are printed as an exhibit to this petition, bound separately, and entitled "Supplement I". The printed report of the Special Master is also furnished as an exhibit, and is entitled "Supplement II".

"S." references are to the material in Supplement I, and "S.M." references are to the Special Master's report, Supplement II. "R." references are to the unprinted record, and are keyed to the items listed in the Praecipe, which is printed at S. 213. The numeral following the letter R refers to the item in the Praecipe bearing that number.

** Earlier opinions of the District Court in this proceeding are reported at 34 F. Supp. 332, 37 F. Supp. 917, and 49 F. Supp. 83.

*Statement of Matter Involved**

This case arises in the Railroad Adjustment Proceeding of The Peoria and Eastern Railway Company, a controlled subsidiary of the Big Four and the New York Central (opinion, S. 14) (the "Operating Companies"), under Chapter XV of the Bankruptcy Act, *infra*, p. 57, as enacted in 53 Stat. 1134 (1939).** The District Court has here allowed against the P & E almost all of a claim of the Operating Companies, over the objections of petitioners, public security holders of the P & E.

Nature and Summary of the Issues

The Operating Companies are fiduciaries of the P & E—they are its majority stockholder, and dominate and control it (*infra*, pp. 9, 21-22), and they operate its railroad as its agent under an Operating Agreement (*infra*, pp. 8-9, 22). They are "self-dealing" fiduciaries—in the many transac-

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* The following abbreviations of names of the parties are used in this petition:

P & E—the respondent, The Peoria and Eastern Railway Company.

Big Four—the respondent, The Cleveland, Cincinnati, Chicago and St. Louis Railway Company.

New York Central—the respondent, The New York Central Railroad Company, controlling stockholder of the Big Four, and after 1930 lessee of its property, including its interest in the P & E (*infra*, p. 9).

Operating Companies—New York Central and Big Four.

Income Bondholders—petitioners, the holders of the P & E's Second Mortgage non-cumulative 4% Income Bonds, due 1990.

** This Chapter XV expired on July 31, 1940, Bankruptcy Act §755 (*infra*, p. 73), but jurisdiction of cases pending on that date (including this case) was reserved by §§746 and 755, *infra*, p. 73.

tions involving both themselves and the P & E, they determine the interests of the P & E as well as their own; that is, they sit on both sides of the table in apportioning the joint revenues and expenses and in otherwise determining the intercompany financial accounts. Their claim here is for advances to cover alleged deficits of the P & E, incurred in the course of such self-dealing (*infra,* pp. 10, 11, 22).

The basic issue in this case is simply whether, as contended by petitioners, these self-dealing fiduciaries are to be held to the usual fiduciary standards, as uniformly laid down in the decisions of this Court—that they must be fair to the P & E, and that *they* have the burden of establishing such fair conduct in the self-dealing transactions (*infra,* pp. 23-25).

The District Court has, in this proceeding under the Bankruptcy Act, repudiated these salutary principles of fiduciary duty (*infra,* pp. 26-27). The Court relied solely upon "presuppositions" assumed by it to be implicit in a preliminary recital to the Operating Agreement, which stated that it would be beneficial if the railroads were under one management (*infra,* p. 31). As will be seen, *infra,* pp. 30-33, the Agreement contains no warrant for relaxing the usual fiduciary standards.

The District Court held that the burden was on the *P & E* to prove that the fiduciaries had mismanaged it for their own benefit, not upon the fiduciaries, the Operating Companies (*infra,* p. 26). The Court also defined the fiduciary standard of conduct at so low a level as to make the burden of proof in effect insuperable. Thus, as to "operating" matters (for example, the routing of traffic) it was held that the fiduciaries could treat the P & E as they would *a wholly owned division,* despite the fact that

it is a separate entity with public security holders. As to "financial" inter-company transactions (for example, apportionment of revenue or expenses) the P & E was held to be entitled not to what was fair in the light of customary railroad practices, but *only* to what it could *prove* it could have exacted if independent, either by sheer weight of its bargaining power or by recourse to the law. The Court then obliterated even this standard as a protection for the P & E, since it, itself, said that there was no way of measuring the P & E's hypothetical bargaining power (*infra*, pp. 27-30).

The claim of the Operating Companies against the P & E for approximately $2,500,000, was, under the Court's standards, upheld except as to a few minor items, upon which they made no defense or but a half-hearted one (*infra*, p. 18), these corrections totaling approximately $130,000 (*infra*, p. 18). Petitioners contend that in many respects the Operating Companies breached the duty required by the usual fiduciary standard of fairness—here customary railroad practice—to which no exception should be made, and that the intercompany accounts should have been adjusted in favor of the P & E in the principal amount of approximately $10,500,000* (*infra*, pp. 40-55). But, of greater importance to the general administration of justice, an acceptance of the principles laid down by the District Court would virtually destroy rules guarding against the excesses of self-dealing corporate fiduciaries, rules which have been built up painstakingly over the years for the protection of public security holders.

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* This amount represented adjustments for the years 1921-1945, inclusive.

Description of the P & E

A brief history of the P & E is essential to an understanding of the issues of this case.

The line of the P & E extends from Indianapolis, Indiana, to the environs of Peoria, Illinois, a distance of 212 miles, and is the direct route between those two important centers. The P & E runs through rich farm lands and serves the thriving industrial areas of Peoria, Danville and Indianapolis, among others. It connects directly with most of the important trunk railroads in the mid-West. It is the only entry of the New York Central system into Peoria, which is one of the three principal gateways between the railroads of the East and those of the West, and which has grown to be one of the largest railroad centers in the country. The P & E handles almost entirely freight traffic (thereby being largely free of the burdens of passenger operations) and has only a main line, with no burdensome branches. (239 I. C. C. 303, at 314; R. 2, pp. 69-71.)

The 1890 Organization of the P & E

The predecessor of the P & E, the Ohio, Indiana & Western Railway, ran from Peoria through Indianapolis, and via its Springfield Division, to Springfield, Ohio (S. M. 3-4). It was reorganized in an equity receivership in 1889-1890, as a result of what the District Court assumed was a "presumably . . . arm's length" (34 F. Supp. 332, 335) deal with the Big Four, although the facts appear to be otherwise.* In any event, as will be seen, this bargain furnished definite advantages to the Big Four.

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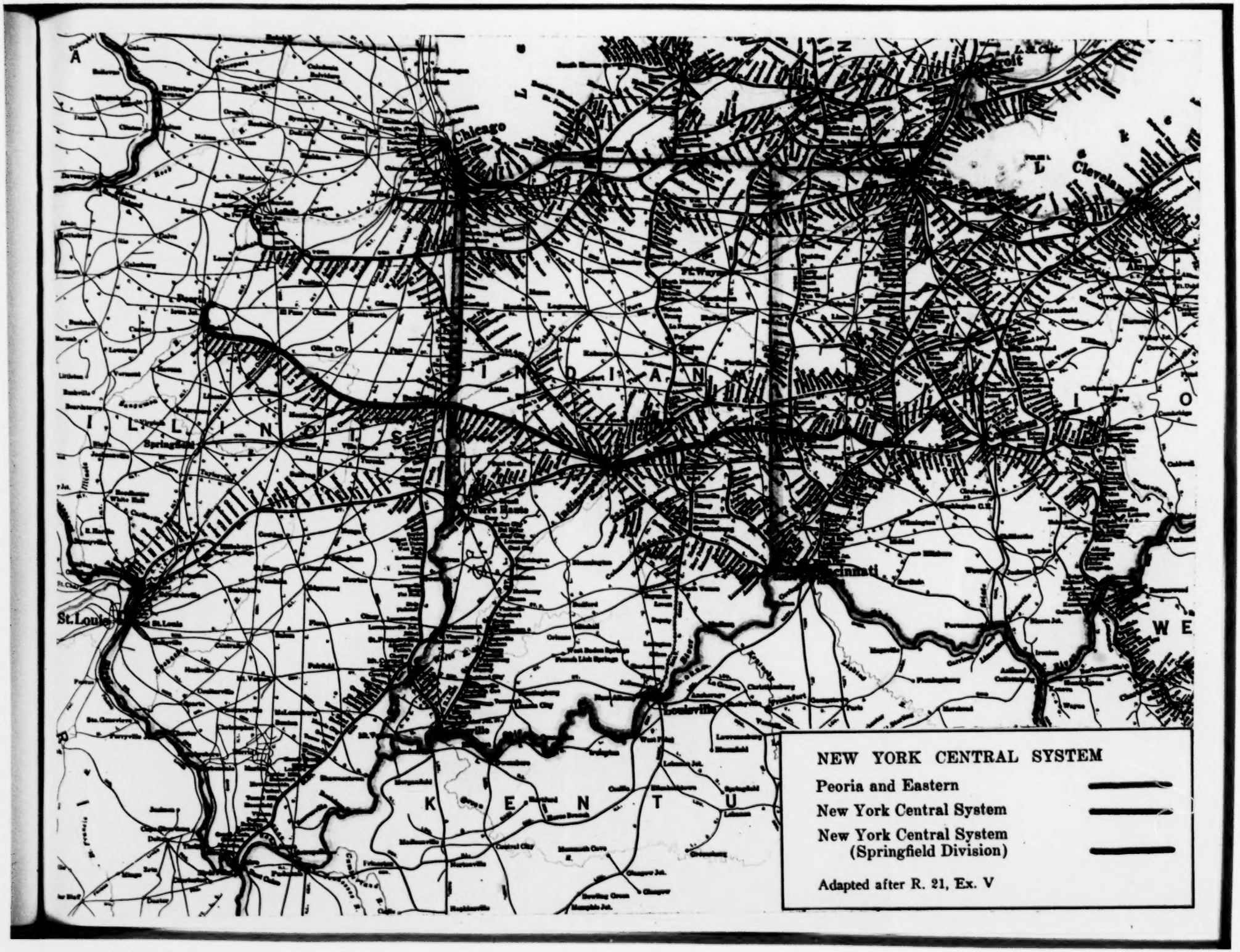
* There is no evidence in the record that this transaction was at arm's length. On the Big Four's side, one of the members of the committee negotiating with the Ohio, Indiana & Western was J. P.


Chicago
Springfield
St. Louis
Cincinnati
Louisville
Cleveland
Detroit
NEW YORK CENTRAL SYSTEM
Peoria and Eastern
New York Central System
New York Central System
(Springfield Division)
Adapted after R. 21, Ex. V

Pursuant to the reorganization, the P & E was organized to take the line from Indianapolis to Peoria. It assumed certain underlying mortgage bonds and issued three classes of securities: (1) First Mortgage 4% Bonds, due 1940 (at which time $8,876,000 in principal amount were outstanding); (2) Second Mortgage non-cumulative 4% Income Bonds in the principal amount of $4,000,000, not due until 1990; and (3) common stock (S. M. 3-4). *The Big Four received 50% of the common stock without paying any cash for it* (S. 119, Finding 16). The other P & E securities were distributed to security holders of the predecessor railroad (R. 23, Ex. 3). (Shortly thereafter the Big Four acquired one additional share of common stock so as to give it a clear majority (S. 120, Finding 17).)

The Big Four, in consideration of thus receiving one-half of the stock of the P & E, agreed (S. 156-158) (1) to purchase the Springfield Division of the Ohio, Indiana & Western (giving to the P & E a purchase money lien for $5,000,000, due in 1940, with interest at 4%, payable annually to the extent that the Division had sufficient earnings (S. 110, Finding 6)); and (2) to operate the P & E for 50 years.

Morgan, a director of the Big Four and senior partner of Drexel, Morgan & Co. (S. 202). The reorganization committee of the Ohio, Indiana & Western consisted of C. H. Coster, Samuel Spencer, George T. Bliss and Anthony J. Thomas (S. 156). Mr. Coster had been a partner of the Morgan firm since 1884 (Satterlee, "J. Pierpont Morgan" (1939), p. 216; Corey, "The House of Morgan" (1930), p. 253-4). Mr. Spencer was the railroad expert for the Morgan firm and became a partner in 1890 (Dictionary of American Biography, "Samuel Spencer", Vol. 17, p. 453-4; Corey, "The House of Morgan" (1930), p. 172). Mr. Bliss was a director of the Big Four (Poor's Manual of Railroads, (1890) p. 993). Mr. Thomas was Vice President of the Big Four's wholly owned subsidiary, the Cairo, Vincennes and Chicago Railway Company (Poor's Manual of Railroads (1889), p. 192 of Appendix).

The Operating Agreement of February 22, 1890 sets forth the obligations of the Big Four assumed in connection with operating the P & E (S. 160-171). A recital in this Agreement stated that it would be beneficial to the business of the railways if they were "put under one management" (S. 162). The term of the Agreement was 50 years from April 1, 1890 "and for such further time thereafter as it [the Big Four] may elect" (S. 162-163, Par. First).

The Operating Agreement provided that the Big Four should "use and operate" the road of the P & E, advancing the costs of operation, maintenance, and equipment (S. 162-163, Par. First). The Big Four agreed that it would advance funds for the payment of interest on the P & E First Mortgage Bonds (S. 163-165, Par. Second). The Big Four was "to receive all earnings and income" of the P & E and apply them in the following order: *First,* to the payment of the operating expenses of the P & E and the interest on the First Mortgage Bonds; *second,* to reimburse itself for any advances made in previous years; *third,* to pay non-cumulative interest up to 4% on the Income Bonds; and *fourth,* to pay the balance to the P & E (S. 165-166, Par. Third). Within 60 days after the end of each year, the Big Four was to furnish a statement of receipts and expenditures of the P & E for the year to the P & E and, on behalf of the P & E, to the Trustee of the Income Bonds (S. 166-167, Par. Fourth). The Big Four was to reimburse itself for accumulated advances (including funds advanced for interest on the First Mortgage Bonds), with interest at 6% per year, only from future earnings of the P & E (S. 167, Par. Fifth; S. 169-171).

Unlike the case of a lease carrying a fixed rental, the financial welfare of the P & E and of its security holders

is dependent upon the operation of the road, and, therefore, upon a fair and honest administration of the Operating Agreement. The Agreement contains no formula for allocating revenues or expenses as between the principal, the P & E, and the operating agent, the Big Four; it also contains no provision as to the fiduciary standards which were to govern in these relations.

Thus, the Big Four, without any cash outlay (except to purchase one share of stock), secured ownership of the Springfield Division, and a majority stock interest in, and operating management of, the P & E. In this way it obtained control of a potential competitor situated in the heart of its territory, furnishing an entrance into Peoria, a gateway to the western railroads.

The Interests in and Manner of Operation of the P & E

From its inception in 1890, the P & E was "completely dominated and controlled" by the Big Four (S. 120, Finding 18). However, over 49% of its common stock was publicly held (239 I. C. C., at 304), as were two issues of bonds, one entitled to fixed interest, and the other, held by the petitioners here, entitled to non-cumulative interest in only such years as the P & E had earnings over and above any accumulated debt to the Big Four.

In 1930 the Big Four leased its property, including its interest in the P & E, to the New York Central, which had secured control of, and dominated, the Big Four (S. 120, Finding 19). *Cf. New York Central Securities Corp.* v. *United States,* 287 U. S. 12 (1932); *New York Central Unification,* 150 I. C. C. 278 (1929).

The P & E was operated, so far as shippers and other railroads were concerned, as an integral part of the Big

Four system, and, after 1930, of the New York Central System (S. 31; S. M. 63). But from an internal financial standpoint, the P & E was a separate railroad with its own security holders (*supra,* p. 7), and it was operated for its own account (S. 160-171). That is, the revenues and expenses attributable to it were supposedly segregated as though it were an independent railroad (S. M. 63, 112). The Operating Companies, in their own names, received these revenues and disbursed the expenditures of the P & E, the latter having never had a treasury of its own (R. 2, p. 149).

The allocation of revenues and expenses by the Operating Companies to the P & E is at the crux of this case. The operation of the P & E involved innumerable transactions between it and the Operating Companies: (1) joint hauls of freight, requiring an allocation of revenue (*infra,* pp. 41-49, 51-52); (2) items of joint expense, to be allocated between them (*infra,* pp. 50-51, 55); (3) leases or sales, e.g., of equipment by the Operating Companies to the P & E, or performance of services by one for the other, requiring the fixing of a proper rental, price or fee (*infra,* pp. 52-54). In every instance, the Operating Companies, and the Operating Companies alone, because of their domination and control of the P & E, allocated the revenues and expenses upon principles determined solely by them (S. 16, 17).

Each year the Operating Companies submitted to the dominated P & E directors a report of the revenues and expenses of the P & E, as determined by the Operating Companies. This report was approved in each case by the P & E directors, and then furnished by the P & E to the Trustee of the Income Bonds, as provided in Section Seventh of the Income Mortgage (S. 19).

The Results of Operations of the P & E (1890-1940)

From the organization of the P & E, no dividends have ever been paid on its common stock. Interest has been paid on the income bonds in only ten years, and not at all since 1913. *Moody's Steam Railroads* (1948) p. 198. And by 1940, the Operating Companies claimed that they were owed approximately $2,500,000, inclusive of interest, for advances made to the P & E to cover the reported deficits determined by them (S. 12; S. M. 7).

Petitioners contend that this poor record of the P & E is an artificial one, due to consistent and recurring patterns of improper allocations of revenues and expenses which were determined in their own interests by the Operating Companies in their "self-dealing" transactions with the P & E. Petitioners contend that upon proper principles, the accounts would show not a debt owed by the P & E, but a sum in excess of $10,500,000 plus interest, owed to it by the Operating Companies.

The 1940 Adjustment

In 1940, the First Mortgage Bonds of the P & E were about to fall due, and the Operating Agreement of 1890 was to expire (S. M. 6, 7).

Pursuant to §710(2) of the Bankruptcy Act, *infra*, p. 59, the P & E filed with the Interstate Commerce Commission an application for authority to modify its securities in accordance with a Plan of Adjustment (239 I. C. C. 303). Under this Plan (S. M. 8), the maturity date of the First Mortgage Bonds was to be extended to 1960, after they were reduced by payment upon them of $4,154,000 (taken from the $5,000,000 to be received from the Big Four

in satisfaction of the purchase money mortgage on the Springfield Division, *supra*, p. 7). The Operating Agreement of 1890 was to be renewed, also until 1960, and the status of the above-mentioned operating debt of $2,500,000, allegedly owed by the P & E to the Operating Companies, was under the Plan to be continued unchanged under the new Operating Agreement (S. 100-107).

No notice of this application to the Commission was given to petitioners, the Income Bondholders of the P & E, and they were not represented at the hearings before the Commission (S. 126, Finding 37), which approved the Plan of Adjustment, *Peoria & E. Ry. Co. Financial Adjustment*, 239 I. C. C. 303 (1940), and also the extension of the Operating Agreement, *Peoria & E. Ry. Co. Operating Agreement*, 239 I. C. C. 320 (1940).

The P & E then instituted the present proceedings in the District Court. A Committee of Income Bondholders was permitted to intervene. It opposed the Plan of Adjustment, arguing, in part, that the claim of the Operating Companies for the $2,500,000 should not be allowed.

The District Court approved the Plan of Adjustment (R. 5-7). *Ewen* v. *Peoria & E. Ry. Co.*, 34 F. Supp. 332 (S. D. N. Y., 1940). However, the Court left open the question whether the claim of the Operating Companies was valid. It said, 34 F. Supp., at page 336:

> "Not only has a large operating deficit accumulated against the Peoria & Eastern, but a large 'retirement' account and a large 'depreciation' account have accumulated in its favor against the New York Central. The plan does not liquidate either of these, and the order of confirmation will leave open all questions touching their amount and validity. If

> the New York Central seeks in any year to withdraw any part of the earnings by way of recoupment, it must prove its right."

The District Court also provided that one director of the P & E should represent the Income Bondholders, in order that they might have "some one who will have the absolute right to scrutinize the road's operation, management and finances." (34 F. Supp., p. 338)

Section 24 of the decree of the Special District Court, as amended in 1941, reads as follows (S. 154):

> "Section 24. All questions concerning the amount and validity of the accounts between the 'Big Four,' the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event, said New York Central Railroad Company and/or 'Big Four,' *upon objection by the representative of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so.*" (Emphasis in original.)

Petitions for certiorari to this Court, raising questions in no way related to those involved in this petition, were denied. 311 U. S. 700 (1940); 314 U. S. 635 (1941).

The Present Controversy

In 1943, the Director of the P & E who represented the Income Bondholders objected to the accounts of the New York Central for the year 1942 (S. M. 16). The Operating Companies then, in accordance with §24 of the decree, just quoted, petitioned in this bankruptcy proceeding for the appointment of a master to hear and report his conclusions as to the amount and validity of the claim of the Operating Companies against the P & E (S. 79-91). This petition also prayed that §24 of the decree approving the Plan of Adjustment be modified as might be just and proper (S. 90-91).

On May 21, 1943, the Special District Court (a) appointed Francis H. Horan, Esq., as Special Master; (b) appointed Charles S. Aronstam, Esq. to represent the interests of the Income Bondholders; and (c) authorized Mr. Aronstam to employ accountants (S. 93). On June 22, 1943, Eppler & Co. (later merged with Peat, Marwick, Mitchell & Co.), a firm of accountants specializing in railroad matters, whose name had been suggested by the New York Central, was employed with the approval of the Special Master, to investigate the inter-company accounts (R. 20, pp. 11-14). On July 2, 1943, the District Court approved the appointment of F. W. H. Adams, Esq., as attorney to represent the P & E (S. 99). Mr. Adams was selected and nominated by the Operating Companies to represent their adversary, the P & E* (S. 12, 94-97; *cf.* S. 91 with S. 97-98). Since January, 1945, Arthur A. Ballantine,

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* The District Court, in appointing the Master, called for an accounting between the P & E and the Operating Companies (S. 93) so that all positions taken by petitioners were necessarily in the interest of the P & E as a whole. Petitioners, on most of the issues before the District Court, were opposed by the P & E, as thus represented by Mr. Adams.

Esq., as the attorney for Mr. Willis D. Wood,* has been associated with Mr. Aronstam in these proceedings (R. 20, pp. 65-66, 136-137).

In 1943, Eppler & Co. made a comprehensive study of the accounts. The Eppler report (R. 21, Ex. A for iden.) found a pattern of error throughout the transactions reflected in the inter-company accounts from 1920 through 1942, arising from deviations from fair and standard railroad practices. The report pointed out that after correcting these errors, the alleged debt to the Operating Companies did not exist, and that they instead owed the P & E some $12,000,000 in principal amount (S. 13). The main items in this report will be discussed, *infra*, pages 41-55.

At the hearings before the Special Master, from February 1945 to August 1946, petitioners' case was presented through the testimony of experts on customary railroad practices.** The Master's report (S. M. 1 *et seq.*) upheld the claim of the Operating Companies with certain relatively minor exceptions.

The District Court, consisting of Circuit Judge L. Hand and District Judges Coxe and Hincks, handed down its opinion per Judge L. Hand, on April 24, 1948, also upholding, to a large extent, the accounts of the Operating Companies (S. 11-68). A limited petition for rehearing

* Mr. Wood and his wife made their original investment in P & E Income Bonds in 1924. They now own $984,000 in principal amount (out of a total issue of $4,000,000 principal amount), of which 80% have been held over 20 years.

** These experts included Mr. R. P. Patterson (recently retired as Freight Traffic Manager of the Pere Marquette Railroad, after 40 years of experience with freight revenue allocations in P & E territory) (R. 20, pp. 3738-3740), Mr. William Wyer (railroad management consultant) (R. 20, pp. 430-432) and members of the staffs of Eppler & Co. (R. 20, pp. 374--382), and Coverdale and Colpitts (engineering consultants) (R. 20, pp. 1177-1180, 1199-1206).

(R. 34) was denied in an opinion on June 4, 1948 (S. 69-73). The final decree, entered on November 16, 1948 (R. 39 or S. 1), amended the decree of July 23, 1940 (S. 10, Sec. 8), as to matters it had left open in otherwise approving the Plan of Adjustment.

The Decision of the Special District Court

The Special Court found that the Operating Companies, through their majority stock interest, "completely dominated" the P & E (S. 14), but that the usual fiduciary duties did not flow from that relationship. This denial of the usual fiduciary duties was based upon the Court's conclusion that the Operating Agreement of 1890 "*presupposed** that the [Operating Companies] should have power to determine the interests of both [the Operating Companies and the P & E] in those mutual transactions" between them (S. 15). This *presupposition*, the Court held, led to two departures from the usual rules as to self-dealing fiduciaries, namely, (1) the standard of duty of the Operating Companies to the P & E was drastically limited, and (2) the burden of proof was placed on the beneficiary, the P & E, and on the Income Bondholders, who asserted its rights, to show that this limited duty was breached (S. 17-18).

The limited standards applied by the Court were as follows:

(1) As to "operating" matters (e.g., the solicitation and routing of traffic, and the selection, maintenance and distribution of equipment), the Operating Companies

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* Throughout this petition, emphasis is added, save where otherwise indicated.

could treat the P & E *as they would a wholly owned division*, and the P & E and the Income Bondholders would have the burden of showing it was treated otherwise (S. 16, 18).

(2) As to "financial" matters (e.g., the allocation of income and expenses), the lower limit of the Operating Companies' permissible conduct was the point at which an independent P & E "would have been unwilling to accept less and would—with possible recourse to the Interstate Commerce Commission—*have been successful in its refusal*" (S. 17). The P & E and the Income Bondholders had the "burden of proof to show that, had the two roads been dealing at arm's length, the 'Peoria' would not have accepted the division made" (S. 18). Further, "In applying this second test", the Court said, "it must always be assumed that management as a single system over which the 'Central' has control is not to be embarrassed" (S. 18).

The Court also held that the annual accounts submitted by the Operating Companies to the P & E were accounts stated, but were voidable by the P & E because of its domination by the Operating Companies (S. 25). However, said the Court, these accounts, as submitted to the Trustee of the Income Mortgage, became accounts stated which concluded the Income Bondholders as to all years prior to 1942, the first year as to which objection was made (S. 21-25).

Lastly, the Court held that the claims of the P & E against the Operating Companies were governed by the New York ten year equity Statute of Limitations (S. 27-29).

The Court, after substituting its own standards for the usual ones, then proceeded to apply them to the individual items of account (S. 29-67). In item after item, as will be seen *infra*, pp. 40-55, the Court concluded that petitioners had failed to sustain their burden of proof to show that the Operating Companies had not lived up to their limited standard of duty. In a few minor respects, mainly where the Operating Companies virtually defaulted,* the Court found errors in the Operating Companies' accounts aggregating $129,468.60, excluding interest (S. 8). The Court also refused to pass upon the merits of two items (and this is not challenged here) on the ground that primary jurisdiction as to them lay in the Interstate Commerce Commission (S. 9-10, Sec. 7(b); S. 56-58, 61-64).

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* The District Court held against the Operating Companies on these matters: (1) On "superimposition", (see p. 44, *infra*) it said that the practice in question was accomplished by formulae "somewhat naively called 'Family Percentages'" by the Operating Companies, and that "so far as we can see, *the 'Central' does not really seek to defend this substitution beyond suggesting that in the end things probably evened up*" (S. 32). (2) On "Grain Transited at Indianapolis and Reshipped to Chicago" (see p. 49, *infra*), the Court found that the Operating Companies had required the P & E to make payments for which they had previously committed themselves, and that it was a practice which *"neither the 'Central' nor the Master seem to defend"* (S. 38). (3) A further error found by the Court in the Operating Companies' accounts was to charge the P & E with the *whole* expense of the freight agencies of the *entire* N. Y. Central System at Indianapolis, Peoria, Pittsburgh and Minneapolis; this the Court termed "the most indefensible act in the whole of the 'Central's' conduct" (S. 41). (4) Charges for Pullman car operations were disallowed, the Court saying that this *"conclusion is not questioned by the 'Central'"* (S. 67).

Jurisdiction

The final decree of the Special District Court was entered on November 16, 1948 (R. 39 or S. 1). The jurisdiction of this Court is invoked under §745 of the Bankruptcy Act, as added by ch. 393 of the Laws of 1939, 53 Stat. 1134, 1141, *infra*, p. 57. Section 745 provides for review directly in this Court of a final decree of the Special Court, on petition for certiorari by any person affected by the plan who deems himself aggrieved.

The present controversy, although postponed to the final stages of this Railroad Adjustment proceeding, is an integral part of it. The Plan of Adjustment of the P & E proposed to leave unchanged the status of this claim of the Operating Companies against it (S. 107). The District Court, however, in its decree approving or modifying other provisions of this Plan, left this portion open and reserved it for future determination (S. 154, §24). The petition of the Operating Companies, initiating the present controversy, prayed that the indebtedness of the P & E to them be settled and stated, and that §24 of the decree approving the plan, be amended (S. 90-91). The final decree of the District Court, settling this intercompany debt, is by its own terms an amendment to the decree approving the Plan (S. 10, Sec. 8).

The validity of this alleged debt is of the essence of the Plan of Adjustment, and whether it is "in the public interest and in the best interests of each class of creditors and stockholders." Bankruptcy Act, §§710 (2)(c)(i), 725 (3), 53 Stat. 1135, 1138, *infra*, pp. 60, 66. The intercompany accounts are, without question, the most important element in the financial condition of the P & E, and therefore affect

all its public security holders. If the balance is as petitioners contend, the Operating Companies owe large sums to the P & E, more than enough to cover its entire funded debt. The principles to be applied in determining the amount and validity of the intercompany accounts are basic in determining the "prospective earnings" of the P & E and indeed in determining its whole future, and therefore the feasibility of this Plan of Adjustment, Bankruptcy Act, §§710(2)(c), 725 (3), 53 Stat. 1135, 1138, *infra*, pp. 60, 66.

Petitioners, the Income Bondholders, are clearly aggrieved by this portion of the Plan. So long as the debt to the Operating Companies exists, the Income Bonds can receive no interest (*supra*, p. 8). Hence they are vitally concerned by a decision allowing the major portion of the claim of the Operating Companies, not only as to the past operations of the P & E, but also for the sanction the decision gives to the same erroneous practices in the future.

Questions Presented

Was the District Court correct in holding, in this proceeding under Chapter XV of the Bankruptcy Act:

1. that (a) as to "operating" matters the Operating Companies could treat the P & E as if it were a wholly owned division and (b) as to "financial" matters the Operating Companies would be found to have breached their fiduciary duties only to the extent that the P & E and the petitioners, the Income Bondholders, could prove that an independent P & E would have refused the allocation of revenue or expense made by the Operating Companies, and would have been successful in its refusal? (See Reason 1, *infra*, pp. 21-34.)

2. that the burden of proof was on the P & E and on the petitioners, the Income Bondholders, to show that the Operating Companies had violated their fiduciary duties in connection with their self-dealing transactions? (See Reason 1, *infra,* pp. 21-34.)

3. that the annual accounts submitted by the P & E to the Trustee of the Income Mortgage were accounts stated which enured to the benefit of the Operating Companies and which precluded the petitioners, the Income Bondholders, from challenging the accounts of the Operating Companies prior to 1942? (See Reason 2, *infra,* pp. 35-37.)

4. that the New York ten-year equity statute of limitations was applicable here? (See Reason 3, *infra,* pp. 38-40.)

5. that the accounts of the Operating Companies were proper, in the respects in which they are challenged by petitioners?* (See Reason 4, *infra,* pp. 40-55.)

Reasons Relied on for Allowance of Writ

1. The Special District Court has decided this case in conflict with decisions of this Court, by failing to hold the Operating Companies to the usual fiduciary standard of fairness in their dealings with the P & E and by placing the burden of proof on the P & E. The decision is of general importance in the fields of securities and bankruptcy law. (Opinion, S. 14-18; Questions 1 and 2, *supra,* pp. 20-21.)

The District Court held that the Operating Companies are fiduciaries of the P & E, because they are its majority

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* The particular facts and issues as to the relevant items in the intercompany accounts are given in connection with the discussion of each item under Reason 4, *infra,* pages 40-55.

stockholders and dominate it. *Southern Pacific Co.* v. *Bogert,* 250 U. S. 483, 487-488 (1919); *Pepper* v. *Litton,* 308 U. S. 295, 306 (1939). This is equally true, since they are its agents in operating its railroad.* *Western Union Tel. Co.* v. *American Bell Tel. Co.,* 125 Fed. 342, 346-347 (C. C. A. 1st, 1903); *Wooton Land & Fuel Co.* v. *Ownbey,* 265 Fed. 91, 99 (C. C. A. 8th, 1920); *The Ticonderoga Railroad Company* v. *The Delaware and Hudson Company,* 204 N. Y. 588, 97 N. E. 475 (1912); *Restatement, Agency* (1933) §13.

The District Court properly found that the claim of the Operating Companies against the P & E arose out of transactions in which there was an absence of arm's length bargaining (S. 14, 16, 17). That is, throughout the existence of the P & E, the Operating Companies have engaged in "self-dealing" in determining what revenues and expenses of their system to ascribe to the P. & E.

The District Court, however, did not give recognition to the legal conclusions which flow, particularly in a court of bankruptcy, from such self-dealing by fiduciaries. This basic error led it to allow the major portion of the claim of the Operating Companies, as is shown, *infra,* pp. 40-55 in the discussion of the objections to the claim.

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* The dominated P & E has acknowledged this agency relationship before this Court. See Brief in Opposition of the P & E in *Gilbert* v. *Peoria and Eastern Railway Co.,* Nos. 466-467, October Term, 1940, at page 26: ". . . the Operating Agreement is not a lease but an agency contract whereby the Big Four without profit undertook to operate the Peoria and Eastern for account of that company under the terms of the Operating Agreement."

This brief was signed by, among others, Jacob Aronson, Esq. as counsel for the P & E. Mr. Aronson was also at that time,and continues to be, Vice President and General Counsel of the New York Central.

a. The Standards Established by this Court, but Rejected Below.

This Court has made it clear that where, as here, arm's length bargaining is missing from intercorporate dealings, it is essential for the appropriate forum to give "rigorous scrutiny" to the transactions in order to protect those interested. *Pepper* v. *Litton,* 308 U. S. 295, 306 (1939); see also *Chelrob, Inc.* v. *Barrett,* 293 N. Y. 442, 57 N. E. (2d) 825 (1944).

In *Schwabacher* v. *United States,* 334 U. S. 182 (1948), this Court, after pointing out that the national transportation policy of the Transportation Act of 1920 required that Federal, not State, law govern mergers of railroads as well as other aspects of the financial condition of the railroads, reemphasized, at page 201, the guiding rule in reviewing such cases as the present one:

> "In determining whether each class of stockholder receives an equivalent of what it turns in, the Commission, of course, is under a duty to see that minority interests are protected, *especially when there is an absence of arm's length bargaining* or the terms of the merger have been imposed by management interests adverse to any class of stockholders."

The applicable rule, stated in *Geddes* v. *Anaconda Mining Co.,* 254 U. S. 590, 599 (1921), to be "founded in soundest morality, and . . . in the soundest business policy", is: the fiduciary is held to a standard of *fairness* in his self-dealing transactions, and the burden of proof is on the *fiduciary* to justify his conduct.

See *Pepper* v. *Litton*, 308 U. S. 295 (1939), where this Court said at pages 306-307:

> "A director is a fiduciary. *Twin-Lick Oil Co.* v. *Marbury*, 91 U. S. 587, 588. So is a dominant or controlling stockholder or group of stockholders. *Southern Pacific Co.* v. *Bogert*, 250 U. S. 483, 492. Their powers are powers in trust. See *Jackson* v. *Ludeling*, 21 Wall. 616, 624. Their dealings with the corporation are subjected to rigorous scrutiny and where any of their contracts or engagements with the corporation is challenged the burden is on the director or stockholder not only to prove the good faith of the transaction but also to show its inherent fairness from the viewpoint of the corporation and those interested therein. *Geddes* v. *Anaconda Copper Mining Co.*, 254 U. S. 590, 599. The essence of the test is whether or not under all the circumstances the transaction carries the earmarks of an arm's length bargain. If it does not, equity will set it aside."

The fiduciary standard of fairness is of especial importance in a proceeding under the Bankruptcy Act, where, as here, the fiduciary is claiming against its beneficiary, the debtor, which is under the protection of the court of bankruptcy. *Pepper* v. *Litton, supra*, 307; *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307 (1939); *Comstock* v. *Group of Investors*, 335 U. S. 211 (1948).

In the *Comstock* case, this Court said at p. 228:

> "a claim against a debtor subsidiary [will] be disallowed or at least subordinated when the claimant corporation has wholly dominated and controlled the subsidiary and in the transactions creating the debt has breached its fiduciary duty and acted both to its own benefit and to the detriment of the debtor."*

* In this case, this Court also said at page 230:

> "The findings here do not stop with holding that the questioned transactions were intended to and did benefit the

The principle that burden of proof is on the fiduciary is also reinforced by the bankruptcy rule, also in conflict with the decision below, that a claimant in bankruptcy has the burden of proof of establishing its claim. *Alexander* v. *Theleman,* 69 F. (2d) 610, 611 (C. C. A. 10th, 1934), cert. denied, 293 U. S. 581 (1934); *In re Annin & Co.,* 95 F. (2d) 381 (C. C. A. 2d, 1938) (Section 77B proceeding); cf. *Whitney* v. *Dresser,* 200 U. S. 532, 534-535 (1906).

In *Alexander* v. *Theleman, supra,* the Court of Appeals said, at page 611:

> "Appellant [a majority stockholder-claimant] carries an additional burden in this case, for the law subjects his dealings in matters where the corporation has an interest to a rigid scrutiny. . . While the sworn statement of the claim is some evidence of its correctness, and is sufficient to carry the burden over formal objection unsupported by proof, Whitney v. Dresser, 200 U. S. 532, 26 S. Ct. 316, 50 L. Ed. 584, the burden is always upon the claimant; when substantial evidence is brought forward to dispute its correctness, the question is, on the entire case including the sworn statement, Has the claim been established? *In this case, on account of the fiduciary relationship of Alexander, that burden was a heavy one before the referee; it is heavier here.*"

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system as a whole. *An over-all benefit to the system might be attained at the injury of one of its units and the security holders of that unit.* But here the finding of good faith and of benefit applies to the New Orleans and its security holders as well as to the system generally."

Compare this with the language of the District Court here: "What was good for the system was by hypothesis good for both; . . ." (S. 42). It should be added that the hypothesis was the District Court's. In each challenged transaction here involved, loss to the P & E meant gain to the Operating Companies.

b. The Rejection of these Fiduciary Standards by the District Court.

These fiduciary rules, though well established, were nevertheless found inapplicable by the District Court (S. 15-18). It relied on the Operating Agreement, which as will be shown *infra*, pp. 30-33, furnishes no justification for this rejection of the usual fiduciary rules. This rejection also finds no warrant in the cases cited above, pp. 23-25, and is therefore in conflict with them.

Thus, the District Court held that the burden of proof was on the P & E (S. 18), and not on the fiduciary-claimant as is required by *Pepper* v. *Litton, supra,* and *Alexander* v. *Theleman, supra.* The District Court accorded similar treatment to the standards of fiduciary duty approved by this Court. These standards, which have never varied in this Court, have not hitherto been thought to be so difficult of application as to require that they be discarded. The District Court, however, specifically turned its back on these tests, after stating them in almost the very words of this Court.

It rejected the test of fairness because it "does not advance to a solution" (S. 15). The doctrine that the fiduciaries should not use their power to the prejudice of the P & E, was disposed of as an "ideal principle" not "capable of application"* (S. 16). And, the Court said, "it is wholly impossible even approximately to set the terms upon which the [operating companies] and the [P & E] would have agreed at arm's length" (S. 17).

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* But compare the language of this Court in *Pepper* v. *Litton,* 308 U. S. 295 (1939) at page 311: "He [the corporate fiduciary] cannot use his power for his personal advantage and to the detriment of the stockholders and creditors no matter how absolute in terms that power may be and no matter how meticulous he is to satisfy technical requirements."

In the place of these tests, the District Court set up a standard of duty for these self-dealing Operating Companies so lenient as to place virtually no restrictions upon them, without the citation of authority for the reduced standards.

The District Court concluded that the fiduciary duties of the Operating Companies differed according to whether they concerned an "operating" or a "financial" matter: (a) as to operating matters—e.g., the solicitation and routing of traffic, schedules, service to shippers or the maintenance and disposition of equipment—the Operating Companies could manage the P & E as they would "a wholly-owned division of [their] system" (S. 18, 16); (b) as to financial matters—e.g., the division of joint revenues and expenses—they could impose terms on the P & E up to the point where, if there had been arm's length bargaining, "the 'Peoria' would have been unwilling to accept less and *would*—with possible recourse to the Interstate Commerce Commission—*have been successful in its refusal;*" (S. 17). This latter test was rephrased in the Court's opinion on rehearing: "whether the 'Peoria', assuming that it was an independent road could have exacted" the terms from the Operating Companies (S. 69). And even this narrow measure of the duty of the Operating Companies to the P & E in "financial matters" was made more rigid by the District Court's holding that "In applying this second test, it must always be assumed that management as a single system over which the 'Central' has control is not to be embarrassed" (S. 18).

Neither branch of the standard established by the District Court conforms to the rule that the Operating Companies must be fair to the P & E.

As to the standard on "operating matters", it is plain that a railroad may act towards a "wholly-owned division"

in any way it sees fit, without regard to any standard, whether of fairness or otherwise. Thus, for example, the power to route traffic involves the power to diminish or increase freight revenues of the P & E *vis a vis* the Operating Companies, and if unchecked (as under the District Court's "operating" standard), ultimately the power to destroy the P & E. The disastrous effects of this standard may be seen, *infra*, pp. 47-48, 52-53, in the discussions of "equalization" and "freight car hire."

Similarly, the District Court's standard on "financial" matters is far removed from one of fairness or arm's length bargaining. In dividing a particular class of revenue or expense there is a range in which arm's length negotiation may operate and agreement may be reached; that is, between the outer limits of an arm's length bargain.* But under the decision of the District Court the P & E, at most, may demand in every instance only the lowest point in this range. That is, the P & E is entitled *only* to what it can prove it could, if independent, *successfully* insist upon by sheer weight of bargaining power, or by recourse to the law.

Further, the District Court indicated in its opinion on rehearing denying "minimums" under its "financial" standard, *infra*, p. 46, that in applying this test, the Operating Companies need only show "that there were a number of cases in which small roads could not" obtain a particular arrangement in order to defeat any claim by the P & E to such an arrangement (S. 70). Thus, the P & E would be entitled in each situation to no more than the

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* Just as there is a zone of reasonableness between the maximum and minimum rate which a carrier is entitled to charge under the Interstate Commerce Act. See *Georgia* v. *Pennsylvania R. Co.*, 324 U. S. 439, 460-461 (1945).

worst treatment received by independent railroads. Even this narrow area for the P & E was obliterated when the District Court concluded, in effect, that the P & E, if independent, would have *no* bargaining power.*

In short, the District Court rejected the standard of fairness, or, as stated by this Court in *Pepper* v. *Litton*, of the "earmarks of an arm's length bargain", because it thought it impossible of application. It substituted its standard of bargaining power, namely, what the P & E could show it could have exacted from the Operating Companies, if independent. On rehearing, the Court found that this test was equally incapable of application, since the bargaining power of the P & E could not be measured. But the Court did not then adopt a workable test—the test, urged by petitioners, of fairness to be found in standard railroad practices; instead the Court held to its unworkable

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* In its opinion on rehearing, the District Court said (S. 70-71):

". . . we must imagine the [P & E], not speaking as a part of a great system, but as a road 212 miles in length which alone had never succeeded in keeping alive. How can we measure the strength of its bargaining power?"

It would be obviously erroneous to conclude that the P & E would have had no bargaining power in 1890 simply because it was then insolvent. Thus, the Ohio, Indiana & Western, the insolvent predecessor of the P & E, had the bargaining power to obtain "minimums" for its Springfield division, as was stated by the District Court in the very next paragraph of its opinion. See footnote, p. 46, *infra*.

The *present* state of the P & E's bargaining power certainly would not follow from its condition in 1890; thus, the Santa Fe, one of the most prosperous and stable railroads today, was in receivership in the 1890's. The territory served by the P & E has grown tremendously, industrially as well as agriculturally, since the 1890's. The decision of the District Court deprives the P & E of any benefits resulting from such growth in its territory, and would actually doom the P & E to the consequences of having had no bargaining power, then or now, for as long as the present Operating Agreement is in force.

test, and because of the erroneously placed burden of proof on the P & E, the P & E was denied any possibility of relief in this proceeding.

The fact that the District Court, under this financial standard, sanctioned unfair treatment of the P & E is clearly shown in its denial of minimums, discussed *infra*, pp. 41-47.

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Under the standards prescribed by the District Court, the Operating Companies are thus given virtually complete power to deal with the P & E as they wish. Certainly, these novel standards of the District Court are entirely foreign to the requirement, established in the decisions of this Court, that a fiduciary must act fairly towards its beneficiary, which, we contend, requires the Operating Companies to follow customary railroad practices in the intercompany dealings.

c. *The Operating Agreement Furnishes No Justification for the Rejection by the District Court of the Usual Rules as to Burden of Proof and the Duty of Fairness Applicable to Fiduciaries.*

The whole answer of the District Court to the application of the usual fiduciary rules as to burden of proof and the duty of fairness was the Operating Agreement (S. 14-18). But there is not a word in that Agreement which warrants any such exception to these rules. The Agreement, of course, contemplated transactions between the P & E and the Operating Companies, but as will be seen, that alone is insufficient to alter the usual fiduciary rules established in this Court. If it were, the law of fiduciary duty, as a protection to corporate minorities, would be set back severely.

The discarding of the usual fiduciary rules was based not upon a specific provision of the Agreement nor even upon inference from a covenant of the Agreement, but flowed from a premise, inferred by the District Court from a *recital* in the Agreement*; the recital, the Court thought, "presupposed that the [Operating Companies] should have the power to determine the interests of" the P & E as well as their own in inter-company transactions (S. 15). This disregards the admonition of *Western Union Tel. Co.* v. *American Bell Tel. Co.*, 125 Fed. 342 (C. C. A. 1st, 1903)** that such a relaxation of fiduciary duty is not to be implied but must be expressly provided in the inter-company agreement.

The District Court, after admitting that it could find no cases "which have explicitly laid down that the burden of

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* The following was the recital relied upon:

"AND WHEREAS the railways of the parties hereto connect at Indianapolis, and it will be beneficial to the business and traffic of said railways that the same be put under one management:" (S. 162).

** Complainant and defendant contracted to consolidate their interests in the telephone business, the defendant to operate the venture and pay royalties to the complainant. In a suit for an accounting, the court held that the defendant was a fiduciary, and "as the sole holder of the joint interests, left in exclusive control thereof, was bound to the underlying rule that neither directly nor indirectly, nor by any artifice whatever, should the [complainant] be deprived of its share in the net profits of the licenses or leases, whatever form they might assume, *unless and except as expressly so provided.*" 125 Fed., pp. 346-347. "The underlying equities which we have described are so strong that they are not lightly to be set aside, *nor can they be ignored on account of mere inferences ingeniously drawn from circumstances,* or from anything except what appears clearly on the face of the contract or what is clearly inconsistent with the operation of its provisions." *Ibid,* p. 350.

proof is on the beneficiary" (S. 18), relied on four cases* as *impliedly* holding that a corporate charter authorizing a fiduciary to self-deal throws the burden of proof on the beneficiary. These cases plainly have no bearing here.

In the first place, none of the cases cited by the District Court concerned the question of burden of proof *in a court of bankruptcy*. Hence, they are insufficient to avoid the bankruptcy rule that burden of proof is on the claimant, which applies even where the claim arose out of arm's length bargaining.

Even apart from the bankruptcy aspects of the present case, the cases cited by the District Court, as it admitted, nowhere state explicitly that burden of proof is on the beneficiary; it is hardly likely that such a grave departure from the usual fiduciary rules would be made in silence. Indeed, in three of them the question could not even have been involved. In two, the *Spiegel* and *Everett* cases, the self-dealing fiduciary was not a party to the litigation, the suit being by stockholders of the beneficiary against the beneficiary's directors**; in the third, the *Goldboss* case, the reference to the exculpatory clause was in connection with a defense of stockholder ratification, not the merits of the

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* *Goldboss* v. *Reimann*, 55 F. Supp. 811 (S. D. N. Y. 1943), aff'd on opinion below, 143 F. (2d) 594 (C. C. A. 2d, 1944); *Spiegel* v. *Beacon Participations*, 297 Mass. 398, 8 N. E. (2d) 895 (1937); *Everett* v. *Phillips*, 288 N. Y. 227, 43 N. E. (2d) 18 (1942); *Helfman* v. *American Light & Traction Co.*, 121 N. J. Eq. 1, 187 A. 540 (Ct. Chancery, 1936). These cases were cited in a footnote of the opinion of the District Court at S. 18.

** This distinction, between the liability of a fiduciary corporation and that of directors of the beneficiary, was made in *Chelrob, Inc.* v. *Barrett*, 293 N. Y. 442, 57 N. E. (2d) 825 (1944), where the Court set aside a transaction as between the corporations, but exonerated the directors of the beneficiary on a finding of good faith.

inter-company transaction. In the fourth, the *Helfman case,* the Court held, at 187 Atl., p. 548, that an exculpatory clause does not "foreclose the court from scrutinizing the . . . transaction as to its fairness."

Thus, the cases cited by the District Court do not warrant its departure from the invariable rule that burden of proof is on the self-dealing fiduciary. *Pepper* v. *Litton,* quoted, *supra,* p. 24. The District Court has plainly misconceived the effect of a mere authorization to self-deal, which is the most that the Operating Agreement is, and which does not affect burden of proof. *Scott on Trusts,* §170.1 (at p. 860). Its only effect is to make the transaction, otherwise absolutely voidable at the option of the beneficiary, merely voidable if unfair. *Jackson* v. *Smith,* 254 U. S. 586 (1921); *Scott on Trusts,* §170.

Similarly, a general authorization to self-deal does not affect the duty of fairness owed by the fiduciary. *Scott on Trusts,* §§170, 216 (p. 1152), 216.3 (p. 1158). The District Court cited no authority for its contrary holding, relaxing this standard. Indeed, at least one of the burden of proof cases it cited, the *Helfman* case, as we have shown, *supra,* this page, expressly held the fiduciary to a duty of fairness. A fiduciary which seeks to be relieved of the usual standard of duty must show a specific provision to that effect; even then, such a provision will be strictly construed. *Western Union Tel. Co.* v. *American Bell Tel. Co.,* 125 Fed. 342 (C. C. A. 1st, 1903), quoted *supra,* p. 31.

d. The Failure of the District Court to Protect the Public Security Holders of the P & E Against the Self-Dealing of the Operating Companies Is of General Importance.

The Court below thus, in effect, emasculated settled fiduciary standards of conduct, and failed to compel the Operating Companies to live up to the duty of fairness established in the decisions of this Court; it did not require the Operating Companies to treat the P & E in accordance with standard railroad practices.

As we have shown, *supra,* page 18, footnote, the practical effect of the District Court's approach was that it ruled against the Operating Companies only where they virtually defaulted in their defense. This is not the "rigorous scrutiny" required by the decisions of this Court. Instead, it is a whitewash on the basis of newly created modifications of fiduciary law, which could produce no other result.

These erroneous conclusions led the District Court into error upon the specific items of account here involved, see pages 40-55, *infra;* but they transcend this particular accounting—they sanction a pattern of overreaching conduct by a dominating stockholder. Any parent, seeking to overreach a subsidiary with public security holders, may have the benefit of this decision by securing from the subsidiary a contract "presupposing" a course of dealings between them.

This decision thus transcends railroad law, and is an undesirable precedent in the fields of general bankruptcy and securities law, as well. It was decided by one of the principal commercial courts of the country, consisting of three judges, one the Chief Judge of the Circuit. It should be reviewed here, the only Court having appellate jurisdiction of the case.

2. The Special District Court went beyond the issues and erroneously held that as to years prior to 1942, the Income Bondholders were precluded from receiving any interest from the P & E because of annual accounts stated and that the Operating Companies were entitled to a credit in the inter-company accounts for any such interest otherwise payable. (Opinion, S. 19-27; Question 3, *supra*, p. 21.)

As we have said above, p. 10, each year the Operating Companies submitted a statement of receipts and disbursements of the P & E to its dominated Board of Directors, who gave their formal approval. These statements, showing since 1913 that no interest was due on the Income Bonds, were also submitted to the Trustee of the Income Bonds.

The District Court properly concluded that as between the Operating Companies and the P & E, there was no binding account stated, because of the domination of the P & E (S. 25).* The Court went beyond the issues of the case, however, to hold that there were annual accounts stated between the P & E and the Income Bondholders for the years prior to 1942, arising from the failure of the Trustee of the Bonds to object to these accounts. This was held to preclude the Bondholders from receiving interest for those years even if the correction of errors in the ac-

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* In fact the Operating Companies, themselves, have never pretended that their statements were final; they have continually made corrections, and properly so, as much as twenty years after the accounts were "stated", as, for example, when in the 1940 accounts there appears the item "Less Adjustment of Interest 1-1-1920 to 12-31-1939" (R. 21, Ex. B; R. 23, Ex. 33t; cf. S. M. 44). At an earlier stage of the proceeding, a memorandum of the P & E to the District Court, dated June 7, 1940, in support of the Plan of Adjustment, said, at p. 36: "The Plan does not contemplate that the amount [of indebtedness of the P & E to the Operating Companies] shown shall be considered as an account stated." This memorandum was signed by Jacob Aronson, Esq., Vice President and General Counsel of both the P & E and the New York Central.

counts would show them otherwise entitled to such interest, and the Operating Companies are to be credited with the amounts of any such interest (S. 26-27). (This ruling was not actually applied in the District Court, since under its decree no interest would have been payable to the Income Bonds in any event. The ruling will be crucial, however, if petitioners prevail in this Court on any of several contentions; it is also of importance for the future not only because it would require the Bondholders, if they were to have any effective protection, to determine to make an annual expensive scrutiny of the complicated accounts and all transactions underlying them within 30 days after their submission, but also for its part in the pattern of domination approved by the District Court.)

The ruling that no interest was payable on the Income Bonds was clearly beyond the issues of this case. The matter in issue in this bankruptcy proceeding was a claim by the Operating Companies against the P & E, the Debtor.* The Income Bondholders took part in this phase of the proceeding only in support of the interests of the P & E, as a whole. There was no dispute between the P & E and the Income Bondholders, and the Court, in its order of reference, tendered no such issue.**

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* The Master was appointed to "hear and report to the Court his findings and conclusions as to the amount and validity of the inter-company accounts between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, The New York Central Railroad Company, and The Peoria and Eastern Railway Company . . . to the end that said inter-company accounts . . . may be settled and stated by this Court . . ." (S. 93).

** The extent to which the District Court departed from the issues actually in the case may be seen in an argument which it stated the petitioners had made—that even though the Bondholders had lost their rights as lienors, they retained rights as unsecured creditors

The Operating Companies had argued, it is true, that there were accounts stated between *them* (not the P & E, as held by the District Court) and the Income Bondholders. This was rejected specifically by the Special Master (S. M. 42) and by implication of silence by the District Court. This argument ignored the fact that there were no contractual relations between the Operating Companies and the Bondholders, and the rule that disabilities of bondholders could not affect the debtor's rights as against the claimants. See *Comstock* v. *Group of Investors,* 335 U. S. 211, 226-227 (1948), where this Court said:

> "We think that, in the reorganization proceeding, the courts may entertain on their merits objections to a plan even if made by one who might be barred from asserting a cause of action in his own behalf, if the subject-matter of the objections is such that it goes beyond the objector's individual interests and affects the fairness and equity of the plan. In view of the amount and position of the claim involved, we do not disagree with the Court of Appeals that such was the case here."

This gratuitous decision of the District Court thus deprived the Income Bondholders of a fair hearing. It was also erroneous and in conflict with decisions of this and other Courts.*

(S. 24). The Bondholders at no time made that argument or anything even remotely resembling it. The District Court apparently confused this case with *Eddy* v. *Prudence Bonds Corp.,* 165 F. (2d) 157 (C. C. A. 2d, 1947), cert. denied, 333 U. S. 845 (1948) where the opinion of the Court, per L. Hand, J., adopted precisely such an argument, the opinion being handed down within two weeks after the instant case was argued orally.

* The decision below failed to recognize that: (1) lack of knowledge by the Trustee and the Income Bondholders of the matters underlying the accounts prevented the existence of accounts stated.

3. The Special District Court erroneously applied the New York ten-year Statute of Limitations, so as to bar correction of the accounts prior to 1933 (Opinion, S. 27-29; Question 4, *supra*, p. 21).

The Special District Court held that this proceeding was in the nature of a minority stockholder's suit to set aside the P & E's consent to the accounts stated, and that it therefore was governed by the New York ten-year equity Statute of Limitations, Civil Practice Act, §53 (S. 27-29). This is a total misconception of the proceeding. It was one to determine the validity of the claim made by the Operating Companies against the P & E, the debtor, in a Chapter XV proceeding. It was therefore not subject to state law in this respect.

This Court held in *Vanston Bondholders Protective Committee* v. *Green*, 329 U. S. 156 (1946), at pages 162-163:

> "In determining what claims are allowable and how a debtor's assets shall be distributed, a bankruptcy court does not apply the law of the state where it sits. *Erie R.R.* v. *Tompkins*, 304 U. S. 64, has no such implication. That case decided that a federal district court acquiring jurisdiction because of diversity of citizenship should adjudicate controversies as if it were only another state court. See *Holmberg* v. *Armbrecht*, 327 U. S. 392. But bank-

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National Surety Co. v. *Manhattan Co.*, 252 N. Y. 247, 169 N. E. 372 (1929); (2) the accounts here could be impeached for fraud or mistake on the part of the P & E, such as was here found to be present. *Oil Co.* v. *Van Etten*, 107 U. S. 325 (1882); (3) railroad accounts at the end of a fiscal year can be at best only approximations since they include accruals for taxes, revenue refunds, employee benefits, etc., and therefore by their own terms such accounts as are here involved do not pretend to be definitive statements upon which a contract fixing the amounts of liability can be based. See footnote, p. 35, *supra*.

> ruptcy courts must administer and enforce the Bankruptcy Act as interpreted by this Court in accordance with authority granted by Congress to determine how and what claims shall be allowed under equitable principles."

The equitable principles for determining whether the Operating Companies' claim should be allowed are not to be circumscribed by *state* Statutes of Limitation, particularly here, where the National Transportation Policy may be involved. See *Schwabacher* v. *United States,* 334 U. S. 182, 191-192 (1948). Thus in *Holmberg* v. *Armbrecht,* 327 U. S. 392 (1946), this Court said at page 396:

> "Traditionally and for good reasons, statutes of limitation are not controlling measures of equitable relief. Such statutes have been drawn upon by equity solely for the light they may shed in determining that which is decisive for the chancellor's intervention, namely, whether the plaintiff has inexcusably slept on his rights so as to make a decree against the defendant unfair. . . .
>
> "Equity eschews mechanical rules; it depends on flexibility. Equity has acted on the principle that 'laches is not like limitation, a mere matter of time; but principally a question of the inequity of permitting the claim to be enforced—an inequity founded upon some change in the condition or relations of the property or the parties."

Here it would be inequitable to allow automatically the claim of the Operating Companies for years prior to 1933, without correction for errors in the very accounts upon which that claim is founded. Hence, the inquiry should go back co-equally to the first transaction giving rise to the claim, i.e., in 1920. *Campbell* v. *Hughes,* 73 Hun 14, 25 N. Y. Supp. 1021 (N. Y. Gen. Term 1893).

Even if the New York Statute of Limitations were applicable, however, the same result would follow. The claim of the Operating Companies is based upon an open account commencing in 1920. Section 56 of the New York Civil Practice Act provides:

> "In an action brought to recover a balance due upon a mutual, open and current account, where there have been reciprocal demands between the parties, the cause of action is deemed to have accrued from the time of the last item proved in the account on either side."

Thus, even under the New York law, the Statute of Limitations commenced to run only after the last item of the account, and barred no part of the case against the Operating Companies.

4. The Special District Court, relying upon its improper rulings of law discussed above, erroneously upheld the accounts of the Operating Companies in many respects (Question 5, *supra*, p. 21).

Petitioners contended in the District Court that the Operating Companies had breached their fiduciary duties in many respects, requiring correction of their accounts in favor of the P & E in the principal amount of approximately $12,000,000. (The items asserted in this Court aggregate approximately $10,500,000.)

The District Court upheld petitioners' contentions to the extent of $129,468.60 in principal amount. As will now be shown, it failed to make other corrections which were urged because it erroneously placed the burden of proof on petitioners, because it adopted incorrect fiduciary standards of duty, or because it improperly applied a ten-year statute

of limitations, all as discussed above in the first and third Reasons for Allowance of the Writ.

a. Freight Revenue (Opinion, S. 29-39, 69-73).

Petitioners' freight revenue claims amount to more than $4,500,000, excluding interest.

i. Minimums (Opinion, S. 34-36, 69-73).

The Operating Companies, in their self-dealing determinations, have consistently depressed the P & E's receipts by denying it a fair share of revenue when the P & E and Big Four are joined in a haul. The Operating Companies have refused to follow customary railroad practices in the determination of such revenues.

The P & E furnishes no transportation service in its own name, being completely submerged in the Big Four so far as shippers or foreign carriers are concerned. Thus, the P & E does not appear as a party in any tariff or division sheets*; the Big Four's tariffs and divisions include the services of the P & E (*supra*, p. 10). On the other hand, the Big Four appears as a separate party from the other parts of the New York Central System in such tariff or division sheets, and is assigned its own divisions of the joint rate as against foreign as well as other system lines (S. 72). Here the question is whether the P & E has received from or through the Big Four a fair share of revenue for its transportation service, in the light of customary railroad practices.

It is the customary practice, where two or more carriers in Official Territory join in a haul of freight, to divide the

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* Further, because the P & E has not been made a party to these tariffs, it was held below that it has no recourse to the Interstate Commerce Commission (S. 31).

joint revenue in the proportion of the mileage each road has contributed to the haul, with certain modifications with respect to the originating and terminating carriers (S. 29-30). The expenses of originating or terminating traffic are high—in the *New York, N. H. & H. R. Co. Reorganization*, 224 I. C. C. 723 (1938), they were found, at page 727, to be equivalent to the cost of hauling the freight 109 miles.*

The originating and terminating carriers customarily receive recognition of these expenses in the form of an added "arbitrary" or "constructive" mileage allowance or a "minimum" share in the joint revenue, if its share otherwise would fall below the minimum. (These practices are further explained in the opinion of the District Court, S. 29-30.) These methods do not furnish exact compensation for these expenses in every case—but it is recognized that in balance they do give a substantial measure of justice as between participating carriers (S. M. 62).

The customary practice of allowing arbitraries and minimums has been confirmed by the Interstate Commerce Commission on many occasions, not only as between independent lines but also in reorganization cases as between divisions of a line. Thus, in the *New York, N. H. & H. R. Co. Reorganization, supra,* the Commission said, at pages 731-732:

> "The principal problem presented in prorating revenues and expenses arising from operations common to two or more lines, or to the system as a whole, is in connection with terminal costs. Such costs gen-

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* These extra expenses were also recognized in, among other cases, *Chicago, R. I. & P. Ry. Co. Reorganization*, 242 I. C. C. 298, 336 (1940), 50 F. Supp. 835, 846 (N. D. Ill., 1943); *New York, S & W. R. Co. Reorganization*, 236 I. C. C. 425, 442 (1939); *Alton R. Co. Reorganization*, 261 I. C. C. 343, 369 (1945).

erally are much higher proportionately than road-haul costs. There are no fixed rules generally in effect for the compensation of terminal lines for these higher costs, *but they always are recognized, in some manner, in the division of interline-freight revenues between different roads.* In some instances a minimum percentage of the rate is allotted to the terminal roads, the residual part being apportioned to the intermediate lines on the basis of mileage. In others a constructive-mileage block is added to the actual mileage of the terminal lines and the revenue is prorated on the basis of the sum of the actual and the constructive mileages."

In *Manistee & Northeastern Ry. Co.* v. *Ann Arbor R. Co.*, 160 I. C. C. 187 (1929), the Commission said, at page 193:

> "The general basis for divisions of rates to and from points in central territory is a mileage prorate, and in calculating mileage for prorating purposes a constructive distance of 100 miles is allowed to the originating or delivering carrier, with minimum of 20 per cent, if the proportion of the haul performed by such carrier is less than that distance."

In *Short Lines' Divisions, Official Territory*, 205 I. C. C. 61 (1934), the Commission said, at page 65:

> "The standard lines deny that there is any single, uniform method but the record indicates that a fairly common basis is a mileage prorate using 50-mile blocks, usually subject to minima for the originating and delivering lines. Frequently the minimum is 20 per cent and sometimes as much as 25 per cent on hauls within the same subterritory of official territory. The minimum is usually lower on hauls to or from other subterritories. For present purposes a

> significant fact is the generally recognized need of some minimum, for, in the nature of things a short line would seldom, if ever, have more than one 50-mile block."

The P & E, which is located in official territory, is charged in the intercompany accounts with *all* the expenses of operating its line, and, therefore, with all its costs of originating and terminating traffic (S. M. 88). Petitioners contend that a fair apportionment of revenue requires that the P & E receive the customary recognition for these added expenses.

In fact, in every case where the P & E is joined with any other road but the Big Four (including direct interchanges with the New York Central proper), the P & E's revenue is determined in accordance with customary practices—on traffic originating or terminating on its line, it receives an arbitrary—so-called block mileage, covering all points within the block, whether or not the shipment traverses the entire block—and where such mileage factor prorated against the mileage factors of the other participating carriers is insufficient to yield it 20% of the revenue it is allowed a 20% arbitrary minimum proportion to protect it against its heavy terminal expenses* (S. 70; S. M. 90). But when, as in the case of 91% of the P & E's traffic to and from the East *the P & E traffic moves over the Big Four* (S. M. 104), the Operating Companies have in the past disregarded both aspects of these customary practices. In determining P & E freight revenues, (1) they "superimposed" their own arbitrary blocks in place of those used in

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* Except as reduced to 19% on shipments to New England. *The New England Divisions Case,* 261 U. S. 184 (1923).

divisions with foreign lines (the "somewhat naively called" family percentages) (S. 31-32; S. M. 64), and (2) they refused to allow any minimums to the P & E (S. 34; S. M. 91). As a result, the P & E's share of a joint rate was on occasion as low as 5.9%, even though it originated or terminated the traffic (S. M. 104).

The District Court held that the first variance from customary practice was improper and that the mileage blocks used by the Big Four in divisions with foreign roads should be followed and the family percentages should not be superimposed (S. 33-34). However, the District Court failed to follow the customary practice of allowing minimums (S. 34-36, 69-73).*

The District Court brushed aside the considerations of fairness as between the P & E and the Operating Companies, and recognition of the P & E's terminal expenses. It applied its "financial" standard—whether an independent P & E could have forced the Operating Companies to grant minimums (S. 17, 69-71). It decided that the P & E, because its predecessor had been in financial difficulties in

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* Petitioners' position on "superimposition" was inseparably tied to the claim for minimums, because, in the absence of knowing what the P & E was entitled to by way of constructive mileage under the division sheets between the Big Four and foreign carriers it was impossible to determine whether or not a minimum was called for under conventional railroad practices. On the accounting, it was found by petitioners that the change in the P & E's freight revenue account resulting from the decision would not be sufficient to warrant the expenditure necessary to determine its precise effect, correcting, as it did, only "superimposition" and not the other aspects of the Operating Companies' failure to follow customary railroad practices (S. 74). Hence, petitioners stipulated that this revision of the intercompany accounts, standing alone, should not be made (S. 74-76).

1890, had no measurable bargaining power* (S. 70-71). It held that this and the fact that the Operating Companies pointed to 34 isolated instances of division sheets since 1880 (R. 23, Exs. 45-56, 204-225) (out of many thousands of such sheets, cf. R. 20, p. 2668) showing minimums for other railroads, but minimums of less than the 20% urged by petitioners, both led to the conclusion that an independent P & E might not have successfully bargained for *any* minimums at all, and so was entitled to none here (S. 70-71).**

The effect of this decision, based upon the improper fiduciary standards laid down by the District Court, is to saddle the P & E with a full load of expenses, while allowing it inadequate revenues to meet such expenses (cf. S. 33). It is little wonder that the P & E has continued to be financially unstable.*** But it is certain these financial

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* The Court ignored the fact that the O. I. & W., the predecessor of the P & E, had the bargaining power to obtain minimums for its Springfield Division, which the Court recognized were still obtained by that Division even though it is wholly owned by the Big Four (S. 71). See footnote at p. 29, *supra*. The O. I. & W. did not need a 20% minimum for shipments to and from the East originating or terminating on that part of its line which became the P & E, since the mileage of that part, in connection with that of the Springfield Division, always resulted in more than the customary 20% minimum.

** The Interstate Commerce Commission has indicated that sheer weight of bargaining power is not relevant to a consideration of a fair apportionment of revenue. Thus, in *Short Lines' Divisions, Official Territory*, 205 I. C. C. 61 (1934), the Commission said, at page 64:

> "In other words, a standard line is clearly not entitled to a more favorable apportionment in dividing with a short line than would be fair in dividing with another standard line."

*** The importance of minimums may be seen by contrasting the P & E with the Springfield Division, both of which were parts of the insolvent O. I. & W. From 1921 to 1940, the P & E, without mini-

machinations do not conform to the standard of public interest, as prescribed by Chapter XV of the Bankruptcy Act.

ii. Equalization (Opinion, S. 36-37).

As we have said, *supra,* p. 44, 91% of the P & E's traffic to or from the East, moves via the Big Four, although, if the P & E were independent, many routes would be available via other railroads, such as the Pennsylvania, the Baltimore and Ohio, the Erie, the Nickel Plate and the Wabash. Frequently, because of circuity of the Big Four route as compared with more direct competing routes, or other circumstances, the proration of the P & E mileage results in a lower share of the joint P & E-Big Four rate to the P & E, than if the shorter competing route (from which the Big Four would have been excluded) were used (S. 36-37). (This is an instance of how the unlimited power to control the routing of the P & E's traffic involves the power to decrease its share of the revenues, and ultimately impoverish it.)

Petitioners contend that while the Big Four may insist on routing the traffic via its own lines, still, as was held in *New York, N. H. & H. R. Co. Reorganization,* 224 I. C. C. 723, 725-726 (1938), the P & E should receive as much revenue from the Big Four as it would have received from shipment via the competing route.

The District Court stated that this contention would be difficult of proof because the shipper (who has ultimate

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mums, was incurring the $2,500,000 deficit claimed here. In that same period, the Springfield Division, with the minimums secured by the insolvent O. I. & W. (S. 71), earned sufficient in *each* year to pay the contingent interest due in connection with the purchase money lien (R. 21, Ex. B).

control of routing) might have chosen the circuitous route (S. 37).* The bondholders' contention was rejected, however, on the sole ground that the Operating Companies under the "operating" standard had the right to choose the route, as if the P & E were a wholly-owned division, and that the P & E was entitled to no more than the share accruing to it according to the route chosen by them (S. 37). Incidentally, this fails to recognize that the District Court, itself, had set different standards for choice of routing (an "operating" matter) and for division of revenues (a "financial" matter). Apart from patently following the wrong one of its own erroneous standards in this financial matter, the District Court erred by not requiring the Operating Companies to sustain the burden of proving that the division of revenues between the P & E and Big Four was fair in such situations, and the *New York, New Haven & Hartford* case, just cited, shows that fairness requires that the principle of equalization be followed.

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* On the other hand, see the decision in *Chicago, B. & Q. R. Co. Control*, 271 I. C. C. 63 (1948), where the Commission said at page 131:

> "Although control is sometimes exercised by consignees over the routing of shipments sold f.o.b. shipping point, the originating carrier controls to a large extent the routing of shipments from industries situated on its line. This is due to the tendency of shippers to patronize the railroad on which they are located and to give it the long haul."

See also pages 152-155 of this opinion.

From the point of view of traffic solicitation and the establishment of routes, the P & E is wholly dependent on the efforts of the Big Four, since it has no traffic department of its own (S. 121, Finding 22).

iii. Grain (Opinion, S. 38).

Petitioners' contentions as to this claim were that similar principles of equalization required an increase in the P & E's share of joint revenue from grain. The District Court rejected these contentions, except in one instance, because of its erroneous conclusion that the Operating Companies could treat the P & E "in the same way that it would, had it been a wholly owned division" (S. 38). The single exception was "Grain Transited at Indianapolis and Reshipped to Chicago," as to which the Court found that the New York Central had saddled the P & E with payments to which it had previously committed itself. The Court stated that the Central did not seem to defend its position as to this (S. 38).

iv. Coal shipments terminating at P & E stations (Opinion, S. 38-39).

Petitioners contended that when coal comes from the Big Four to the P & E and terminates at its stations, the P & E was allocated too small a portion of the joint rate. Although the District Court indicated that the amounts allocated to the P & E were improper (on the same basis as "superimposition") it rejected the claim on the ground that the P & E did not meet its burden of proof by showing the basis on which the joint rates were divided. This failure was due to the fact that the Operating Companies had lost the "authority files"* (S. 39).

This decision illustrates the logical absurdity of the Court's ruling on burden of proof. One of the reasons for

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* The exchange of letters between the interested railroads by which the division of revenue contracts had been negotiated and agreed upon.

placing the burden of proof on the fiduciary is that it has control of the records underlying its conduct; it should bear the burden of loss of the records.

b. Traffic Expenses (Opinion, S. 40-41).

The Operating Companies have always charged the P & E with a proportion of the traffic expenses of the entire system (determined on a pro rata revenue basis); and until 1935 they charged it with the entire cost of the system offices at Indianapolis, Peoria, Pittsburgh and Minneapolis.

Petitioners contended that in numerous instances the System's traffic department had solicited and routed traffic so as to benefit the Operating Companies and harm the P & E, even to the extent of excluding the P & E from traffic of industries on its lines;* that the burden was on the Operating Companies to show that the traffic department had benefited the P & E so as to entitle them to charge the P & E for these traffic expenses; and that because of their failure to show any benefit, they were not entitled to any of the

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* Thus, the traffic department (1) diverted brick traffic originating *on the P & E's line* in Danville to other system lines by refusing to open more direct P & E routes (R. 20, pp. 997-1009); (2) failed to open through routes from many Big Four stations to Western Trunkline territory via the P & E although this was often the direct route (R. 20, pp. 1009-1026); (3) routed only 6.6% of the system controlled traffic from Indianapolis to St. Louis, Chicago and western points via the P & E, although practicable P & E routes were available (R. 21, Exs. PPPP, ZZZZ; R. 20, pp. 1027, 1042, 1052-1053, 1061); (4) solicited P & E traffic for a long haul over other system lines, because this involved substantial revenue benefit to the system although it resulted in substantial loss to the P & E (S. 36-37; *supra*, pp. 44-45, 47-48). In addition, the traffic department made no attempt to obtain minimums for the P & E when the Big Four was joined in the haul although the P & E paid all its terminal expenses (S. 34; *supra*, p. 44).

claimed expenses. *Cf. Bibb* v. *Allen,* 149 U. S. 481, 498 (1893). This claim amounts to approximately $1,500,000.

The District Court without mentioning any of the specific instances of misconduct cited by petitioners, said that the claim of misconduct was without substance (S. 40). This holding was undoubtedly based on the Court's erroneous conclusions that the burden of proof was on the P & E and petitioners, and that as to operating matters, the Operating Companies could treat the P & E as a wholly-owned division (since the functions of the traffic offices and the misconduct cited by petitioners are "operating" matters within the Court's definition). The District Court, however, disallowed the Operating Companies' practice of charging the P & E with the entire expense of the system traffic offices at Indianapolis, Peoria, Minneapolis and Pittsburgh for the years 1933 and 1934, holding that the claim for earlier years was barred by the Statute of Limitations (S. 41).

c. *Harrisburg Coal Moving Overhead on the P & E (Opinion, S. 41-42).*

Petitioners contended that on certain coal traffic originating on the Big Four at the Harrisburg, Illinois, coal fields, and interchanged with the P & E at Danville for shipment through Peoria to the West, the revenue assigned by the Operating Companies to the P & E was insufficient to cover its out-of-pocket costs; that the Big Four was willing to take this traffic at a loss, since it received other benefits from this traffic (an on-line source of coal, and the general freight traffic of the mining communities), not shared by the P & E; and that fairness required that the P & E receive a larger return for its carriage of this traffic

(S. M. 151). This claim amounted to approximately $1,700,000.

The District Court rejected (S. 42) this contention for the same erroneous reasons as led it to reject "equalization", *supra,* pages 47-48.

d. Freight Car Hire (Opinion, S. 43-50).

Railroads exchange freight cars freely, the road having possession of a car paying to the owner a daily rental fee, known as a "per diem". This per diem is paid whether the car is loaded or empty, moving or stationary. When an empty car is homeward bound, these per diems continue; but any road which did not participate in the last revenue haul of the car, i.e., one over which the car does not have "record rights", is entitled to charge a six cents per mile fee for hauling the empty car (S. 43-44).

The P & E pays and receives per diems *vis a vis* the Operating Companies as though they were foreign roads. However, for purposes of determining record rights, the P & E is considered a part of the New York Central system —it does not collect or pay a haulage fee if the car belongs to the New York Central system or belongs to a foreign road and has record rights over the system (S. 44).

Petitioners contended in the District Court that the Operating Companies imposed excessive per diems upon the P & E in two major respects: First, in causing system cars to be stored empty on the P & E, incurring large per diems;* and, second, in requiring the P & E to haul without

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* While the system made countervailing credits on certain of these "stored" cars, these storage credits were made at the discretion of system officers and only on certain cars. The storage credit arrangement was acknowledged by a responsible system official to be unfair (S. 45; S. M. 202).

compensation system cars or other cars having record rights over the system (but not the P & E), the P & E, all the while, paying per diems on these cars. Petitioners introduced into evidence a study showing that in a single month, January, 1940, the P & E paid a net amount of $1,313 in per diems in connection with 492 New York Central System empty cars, none of which had been used or was thereafter used in the service of the P & E (S. M. 197; S. 47). Petitioners' claim was for approximately $670,000.

The District Court recognized that the burden on the P & E "was of substantial dimensions and was one that if independent it could have escaped" (S. 47). However, it held that as an operating matter, the Operating Companies could adopt these freight car practices as if the P & E were a wholly owned division and that they "may have been of benefit to the" P & E; that the petitioners had failed to meet their burden of proof* of showing a breach of duty by the Operating Companies, particularly from the point of view of fixing damage to the P & E; and that a part of this claim was barred by the Court's rulings as to account stated and Statute of Limitations (S. 43-50). Here again the decision of the Court has an important bearing on the future operation of the P & E, and thus on the fairness and feasibility of the Plan of Adjustment.

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* The Special Master said "They [the Bondholders] have brought forward enough data, which has not been adequately explained to make it impossible to say categorically that the P & E may not at times have been unfairly treated in the matter of per diems" (S. M. 206).

e. Sale of Second Hand Equipment (Opinion, S. 52-55).

Petitioners contended that the Operating Companies had sold old, obsolescent* equipment to the P & E for excessive prices, their claim amounting to approximately $450,000. As to petitioners, the Court rejected the contention because of its erroneous ruling as to accounts stated. As to the P & E, the Court held that as an "operating" matter, the Operating Companies might sell second hand equipment to the P & E, and that the burden of proof was on the P & E to show an excessive price. The Court held that this erroneously placed burden had not been sustained as to all but one of the sales, and as to some of the sales, that the Statute of Limitations was a bar. (S. 52-55.)

f. Champaign Grain Elevator (Opionion, S. 60).

Petitioners contended, and the Special Master found (S. M. 280), that in 1916 the Big Four improperly sold the P & E a grain elevator, this being not an expenditure for railroad purposes. This claim was for approximately $115,000, paid over the years 1920-1926. The District Court erroneously refused to pass on this contention on the ground that it was barred by its rulings as to account stated and Statute of Limitations (S. 60).

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* This, in turn, tended to add to the cost of repairing the equipment, which was the subject of another contention of petitioners, who showed that the cost of freight car repairs charged in their accounts by the Operating Companies against the P & E exceeded the average cost for class I railroads by over 44%. The District Court rejected petitioners' contention that these costs were excessive on the ground that petitioners had failed to carry the burden of proof erroneously placed on them (S. 50-51).

g. General Expenses (Opinion, S. 65-67).

Petitioners contended that the Operating Companies charged the P & E with an excessive share of general expenses, these averaging 40% more than the expenses of comparable railroads,* and that certain expenses for the salaries of general officers should be disallowed in their entirety since they had not acted loyally and in good faith to the P & E. This claim was for approximately $1,565,000. The District Court rejected the first of these contentions because of failure to sustain the erroneous burden of proof placed on petitioners, and the second for the same erroneous reasons as traffic expenses, *supra*, pp. 50-51. S. 65-67.)

CONCLUSION

We have shown that the District Court applied erroneous fiduciary standards in this case, in conflict with settled principles laid down in the decisions of this Court. These basic errors make this case one of general importance in the fields of bankruptcy and securities law, which, if unreversed, will be a constant invitation to similar overreaching.

Had the District Court not applied the erroneous fiduciary standards governing the duties of the Operating Companies to the P & E, not only would the claim of the Operating Companies, amounting to approximately $2,500,000, have been disallowed, but a correction of approximately

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* The Special Master concluded "the whole of the general expenses, including the Indianapolis costs, are relatively so heavy as to invite criticism. The explanations of the Central have *just about rebutted* the inference that there has been negligent operation at the Indianapolis office" (S. M. 293).

$10,500,000, plus interest, in favor of the P & E would have been required.

WHEREFORE, it is respectfully submitted that this petition for certiorari to review the final decree of the Special District Court for the Southern District of New York should be granted.

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APPENDIX

Statutory Provisions

Pertinent statutory provisions are as follows:

53 Stat. 1134 (1939)

[Chapter 393]

AN ACT

To amend an Act entitled "An Act to establish a uniform system of bankruptcy throughout the United States", approved July 1, 1898, and Acts amendatory thereof and supplementary thereto.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Act of July 1, 1898, entitled "An Act to establish a uniform system of bankruptcy throughout the United States", as amended, is hereby further amended by adding thereto a new chapter, to be designated chapter XV, and to read as follows:

"CHAPTER XV—RAILROAD ADJUSTMENTS

"ARTICLE I—JURISDICTION

"SEC. 700. In addition to the jurisdiction otherwise exercised, courts of bankruptcy shall exercise original jurisdiction, as provided in this chapter, for postponements or modifications of debt, interest, rent, and maturities or for modifications of the securities or capital structures of railroads.

"ARTICLE II—DEFINITIONS

"SEC. 705. The following terms, as used in this chapter, unless a different meaning is plainly required by the context, shall be construed as follows:

"(1) 'Petitioner' means any carrier as defined in section 20a of the Interstate Commerce Act, excluding any corporation in equity receivership or in proceedings for reorganization under section 77 of this Act, petitioning for a plan of adjustment, as hereinafter defined.

"(2) 'Claims' includes debts whether liquidated or unliquidated, certificates of deposits of securities (other than stock and option warrants to subscribe to stock), including demands and obligations of whatever character made, assumed or guaranteed by the petitioner.

"(3) 'Debt' shall be considered to include all claims held or owned by 'creditors' as hereinafter defined.

"(4) 'Creditors' shall include all holders of claims, demands, and obligations of whatever character against the petitioner or its property, whether or not such claims would otherwise constitute provable claims in bankruptcy, including the holders of claims made, assumed, or guaranteed by the petitioner.

"(5) 'Securities' shall include those defined in section 20a of the Interstate Commerce Act, as amended, and also certificates of deposit and all other evidences of ownership of or interest in securities.

"(6) 'Commission' refers to the Interstate Commerce Commission.

"(7) 'Adjustment' shall include postponements or modifications of debt, interest, rent, and maturities and modifications of the securities or capital structures.

"SEC. 706. No creditor shall be deemed to be 'affected' by any plan unless such plan proposes a modification of the evidence of debt or other instrument defining the rights of such creditor, or a modification of the security, if any, for the claim of such creditor.

"ARTICLE III—PETITION AND POWERS OF COURT

"SEC. 710. Any railroad corporation not in equity receivership or in process of reorganization under section 77 of the Bankruptcy Act at the time of filing its petition hereunder, and which has not been in equity receivership or in process of reorganization under said section 77 within ten years prior to the filing of such petition, which shall have—

"(1) Prepared a plan of adjustment and secured assurances satisfactory to the Commission of the acceptance of such plan from creditors holding at least 25 per centum of the aggregate amount of all claims affected by said plan of adjustment (including all such affected claims against said corporation, its parents and subsidiaries), and

"(2) Thereafter obtained an order of the Commission, (but not of a division thereof), under section 20a of the Interstate Commerce Act authorizing the issuance or modification of securities as proposed by such plan of adjustment (other than securities held by, or to be issued to Reconstruction Finance Corporation),

such order of the Commission to include also specific findings:

"(a) That such corporation is not in need of financial reorganization of the character provided for under section 77 of this Act;

"(b) That such corporation's inability to meet its debts matured or about to mature is reasonably expected to be temporary only; and

"(c) That such plan of adjustment, after due consideration of the probable prospective earnings of the property in the light of its earnings experience and of such changes as may reasonably be expected,—

"(i) is in the public interest and in the best interests of each class of creditors and stockholders;

"(ii) is feasible, financially advisable, and not likely to be followed by the insolvency of said corporation, or by need of financial reorganization or adjustment;

"(iii) does not provide for fixed charges (of whatsoever nature including fixed charges on debt, amortization of discount on debt, and rent for leased roads) in an amount in excess of what will be adequately covered by the probable earnings available for the payment thereof;

"(iv) leaves adequate means for such future financing as may be requisite;

"(v) is consistent with adequate maintenance of the property; and

"(vi) is consistent with the proper performance by such railroad corporation of service to the public as a common carrier, will not impair its ability to perform such service:

Provided, That in making the foregoing specific findings the Commission shall scrutinize the facts independently of the extent of acceptances of such plan and of any lack of opposition thereto: *Provided further,* That an order of the Commission (or of a division thereof) under section 20a of the Interstate Commerce Act, made prior to April 1, 1939, authorizing the issuance or modification of securities as proposed by a plan of adjustment (other than securities held by, or to be issued to, Reconstruction Finance Corporation), shall be effective for the purpose of this subparagraph (2) of the first sentence of section 710, notwithstanding failure to include therein the foregoing specific findings, if such order did include the specific findings that such proposed issuance or modification of securities is compatible with the public interest, is consistent with the proper performance by the railroad corporation of service to the public as a common carrier, and will not impair its ability to perform such service, and

"(3) Secured assents to such plan of adjustment by creditors holding more than two-thirds of the aggregate amount of the claims affected by said plan, which two-thirds shall include at least a majority of the aggregate amount of the claims of each affected class,

may file in the United States district court in whose territorial jurisdiction such railroad corporation has had its principal executive or principal operating office during the

preceding six months or a greater period thereof, its petition averring that it is unable to meet its debts, matured or about to mature, and desires to carry out the plan of adjustment.

"A copy of the order obtained from the Commission, as above provided, shall be filed with the petition and made a part thereof.

"SEC. 711. Any corporation which has complied with subparagraphs (1), (2), and (3) of the first sentence of section 710, and in which corporation the majority of the capital stock having power to vote for the election of directors is owned, directly or indirectly through an intervening medium by any railroad corporation which has filed a petition hereunder, or any corporation which is a lessor of the petitioning corporation and which has complied with the aforesaid subparagraphs (1), (2), and (3) of section 710, may file its petition in the same court in which the petition first aforesaid shall have been filed, and such petitions shall be heard and disposed of in a single proceeding.

"SEC. 712. The petition shall be accompanied by payment to the clerk of a filing fee of $100, which shall be in addition to the fees required to be collected by the clerk under other sections of this Act, or any other Act.

"SEC. 713. Immediately following the filing of the petition, there shall be convened a special court of three judges in the manner provided by section 266, as amended, of the Judicial Code, and thereafter all proceedings relative to such plan or any modification thereof shall be conducted before such court. Such three-judge court shall be vested with and shall exercise all the powers of a district court

sitting in equity and all the powers as a court of bankruptcy necessary to carry out the intent and provisions of this chapter, including the classification of claims at such time and in such manner as the court may direct.

"SEC. 714. The special court, after hearing, promptly shall enter an order approving the petition as properly filed under this chapter if satisfied that such petition complies with this chapter and has been filed in good faith, or dismissing such petition if not so satisfied.

"SEC. 715. If the petition is approved by the special court, the said court, during the pendency of the proceedings under this chapter, shall have exclusive jurisdiction of the petitioner and of its property wherever located to the extent which may be necessary to protect the same against any action which might be inconsistent with said plan of adjustment or might interfere with the effective execution of said plan if approved by the court, or otherwise inconsistent with or contrary to the purposes and provisions of this chapter: *Provided, however,* That nothing herein contained shall be construed to authorize the court to appoint any trustee or receiver for said properties or any part thereof, or otherwise take possession of such properties or control the operation or administration thereof.

"ARTICLE IV—HEARINGS

"SEC. 720. The special court shall fix a date for a hearing to be held promptly after the filing of the petition and notice of such hearing or hearings shall be given to all persons in interest in such reasonable manner as the court shall direct. In such proceeding, the court may allow such

interventions of persons in interest as it may deem just and proper, but any person in interest shall have the right to present evidence and be heard thereon, in person or by attorney, with or without intervention.

"SEC. 721. After such hearing, the special court may approve the plan as filed or propose to modify such plan and as hereinafter provided approve the same as so modified. If the court shall propose to modify the plan, then: (a) if such modification substantially alters the basis for the specific findings included in the order made by the Commission under section 20a of the Interstate Commerce Act, the plan as so proposed to be modified shall be resubmitted to the Commission and shall not be finally approved by the court until the Commission (but not a division thereof) has authorized the issuance or modification of securities as proposed by the plan as so modified (other than securities held by, or to be issued to, Reconstruction Finance Corporation) making the findings required by clause (c) of subparagraph (2) of the first sentence of section 710, even in a case where the original order of the Commission under said section 20a was made prior to April 1, 1939; and (b) if such modification substantially or adversely affects the interests of any class or classes of creditors, such plan shall be resubmitted, in such manner as the court may direct, to those creditors so affected by such modification and shall not be finally approved until after (1) a hearing on such modification, to be held within such reasonable time as the court may fix, at which hearing any person in interest may object to such modification, and (2) a reasonable opportunity (within a period to be fixed by the court), following such hearing, within which such affected creditors who have assented to

the plan may withdraw or cancel their assents to the plan, and failure by any such creditor to withdraw or cancel an assent within such period shall constitute an acceptance by such assenting creditor of the plan as so modified. After such authorization and finding by the Commission, where required hereby, and after such hearing and opportunity to withdraw or cancel, where required hereby, the court may make the proposed modification, and as provided in section 725 finally approve and confirm the plan as so modified.

"SEC. 722. If the United States, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States, is a creditor or stockholder, the Secretary of the Treasury is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation . If in any proceeding under this chapter the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in or claim against the debtor as creditor or stockholder), no plan which does not provide for the payment thereof shall be approved by the court except upon the acceptance of a lesser amount or of a postponement by the Secretary of the Treasury certified to the court: *Provided,* That if the Secretary of the Treasury shall fail to accept or reject such lesser amount or such postponement for more than sixty days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as its claims for taxes or customs duties are concerned shall be conclusively presumed.

"ARTICLE V—PROCEEDINGS SUBSEQUENT TO APPROVAL OF PETITION

"SEC. 725. If the special court shall find—

"(1) That, at the time of the filing of said petition as provided in article III hereof, the proposed plan of adjustment had been assented to by not less than two-thirds of the aggregate amount of all claims of the petitioner affected by such plan, including at least a majority of the aggregate amount of claims of each such class;

"(2) That the plan of adjustment as submitted or as modified by the court has been accepted or, if modified, then as modified by or on behalf of creditors affected by such plan holding more than three-fourths of the aggregate amount of the claims affected by said plan, including at least three-fifths of the aggregate amount of the claims of each affected class;

"(3) That the plan meets the requirements of clause (c), and the petitioner meets the requirements of clauses (a) and (b) of subparagraph (2) of the first sentence of section 710, and that the plan is fair and equitable as an adjustment, affords due recognition to the rights of each class of creditors and stockholders and fair consideration to each class thereof adversely affected, and will conform to the law of the land regarding the participation of the various classes of creditors and stockholders: *Provided,* That in making the findings required by this clause (3), the court shall scrutinize the facts independently of the extent of acceptances of such plan, and of any lack of opposition thereto, and of the fact that the Commission, under

section 20a of the Interstate Commerce Act, has authorized the issuance or modification of securities as proposed by such plan, and of the fact that the Commission has made such or similar findings;

"(4) That all corporate action required to authorize the issuance or modification of securities pursuant to such plan shall have been duly taken;

"(5) That the petitioner has not, in connection with said plan or the effectuation thereof, done any act or failed to perform any duty which act or failure would be a bar to the discharge of a bankrupt, and that the plan and the acceptance thereof are in good faith and have not been made or procured by any means, promises, or acts forbidden by this Act; and

"(6) That, after hearings for the purpose, all amounts or considerations, directly or indirectly paid or to be paid by or for the petitioner for expenses, fees, reimbursement or compensation of any character whatsoever incurred in connection with the proceeding and plan, or preliminary thereto or in aid thereof, together with all the facts and circumstances relating to the incurring thereof, have been fully disclosed to the Court so far as such amounts or considerations can be ascertained at the time of such hearings, that all such amounts or consideration are fair and reasonable, and to the extent that any such amounts or considerations are not then ascertainable, the same are to be so disclosed to the Court when ascertained, and are to be subject to approval by the special court as fair and reasonable, and except with such approval no amounts or considerations covered by this clause (6) shall be paid.

Said court shall file an opinion setting forth its conclusions and the reasons therefor and shall enter a decree approving and confirming such plan and the adjustment provided thereby, which decree shall be binding upon the petitioner and upon all creditors and security holders of the petitioner; and thereafter the petitioner shall have full power and authority to and shall put into effect and carry out the plan and the orders of the special court relative thereto and issue the securities provided by the plan without further reference to or authority from the Commission or any other authority, State or Federal, except where required by any law relating to the Reconstruction Finance Corporation, and the rights of all creditors and security holders with respect to claims and securities affected by the plan shall be those provided by the plan as so approved and confirmed: *Provided, however,* That the title of any owner, whether as trustee or otherwise, to rolling-stock equipment leased or conditionally sold to the petitioner, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this chapter.

"No plan shall be approved under this chapter unless the special court finds that with respect to the continuation of, or any change in, the voting rights in the petitioner, control of the petitioner, and the identity of, and the power and manner of selection of the persons who are to be directors, officers, or voting trustees, if any, upon the consummation of the plan and their respective successors, the plan makes full disclosure, is adequate, equitable, in the best interests of creditors and stockholders of each class, and consistent with public policy.

"SEC. 726. After the special court shall have approved as properly filed a petition pursuant to article III hereof, the special court, from time to time during the pendency of the proceedings hereunder, may enjoin the institution of, or stay, for a reasonable time, any action or proceeding to enforce any right against the petitioner or its property based upon claims affected by the proposed plan of adjustment in any court, State or Federal, whether for the enforcement of any such claim or for the appointment of receivers in equity or of the institution or prosecution of a proceeding under section 77 of the Bankruptcy Act or otherwise: *Provided, however,* That no such stay shall affect any proceeding based on or to enforce any claim which would be required to be paid if the plan of adjustment proposed by the petitioner were then in effect.

"SEC. 727. Unless the plan of adjustment as submitted or as modified shall have been confirmed by the special court within one year from the date of filing the petition, the proceedings shall be dismissed unless, for good cause shown, on motion of any party in interest the court, if satisfied that confirmation of a plan is in immediate prospect shall determine otherwise.

"SEC. 728. Without prejudice to existing rights of all creditors, including those affected by the plan, and as a condition to the approval of any plan by the special court, the petitioner, from and after the filing of the petition with the court and until the making of a final order by the special court approving a plan or dismissing the petition, shall continue to make or tender payment to all creditors affected by the plan of sums currently payable to such creditors equal to the amounts proposed to be paid to such creditors under the plan: *Provided,* That the making of

such payments shall not constitute a preference within the meaning of the Bankruptcy Act, nor shall acceptance of such payments constitute an acceptance of a plan. If, from and after the filing of the petition with the special court, there shall be any failure to make or tender such payments, the special court, unless there is good cause shown for the failure, shall dismiss the proceedings. In finally approving any plan, the court may make or require to be made such adjustments with respect to said payments or any of them as may be necessary to make the same conform to the provisions of said plan as finally approved.

"SEC. 729. In providing for any such payments the petitioner may require any bond or other security, including interest coupons affected by such payments to be presented to or deposited with a paying agent or depositary named by the petitioner for appropriate stamping to show the amounts of such payment.

"ARTICLE VI—TAX PROVISIONS

"SEC. 735. The provisions of Sections 1801, 1802, 3481, and 3482 of the Internal Revenue Code and any amendments thereto, unless specifically providing to the contrary shall not apply to the issuance, transfer, or exchange of securities or the making or delivery of conveyances to make effective any plan of adjustment confirmed under the provisions of this chapter. No income, gain, or profit taxable under any law of the United States or of any State, now in force or hereafter enacted, shall in respect to the adjustment of the indebtedness of any petitioner in a proceeding under this chapter be deemed to have accrued to or to

have been realized by such petitioner by reason of a modification of or cancelation in whole or in part of any of the indebtedness of the petitioner affected by a proceeding under this chapter.

"SEC. 736. In addition to the notices elsewhere expressly provided, the clerk of the court in which any proceedings under this chapter are pending shall forthwith transmit to the Secretary of the Treasury copies of—

"(1) Every petition filed under this chapter;

"(2) The orders approving or dismissing petitions;

"(3) The orders approving plans as filed or as modified, together with copies of such plans as approved;

"(4) The decrees approving and confirming plans and the adjustments provided thereby, together with copies of such plans as approved;

"(5) The injunctions or other orders made under section 726 of this chapter;

"(6) The orders dismissing proceedings under this chapter; and

"(7) Such other papers filed in the proceedings as the Secretary of the Treasury may request or which the court may direct to be transmitted to him.

"SEC. 737. Any order fixing the time for confirming a plan which affects claims or stock of the United States shall include a notice of not less than thirty days to the Secretary of the Treasury.

"SEC. 738. The special court shall have power to determine the amount and legality of claims of the United

States for taxes or customs duties, and to order payment thereof; and the order of the special court (provided for in section 714) approving the petition shall have the effect of an adjudication of bankruptcy of the petitioner for the purposes of section 274 of the Internal Revenue Code and the corresponding provisions of prior and subsequent revenue acts. The running of the statute of limitations on the assessment or collection of any internal-revenue tax shall be suspended while a proceeding under this chapter is pending and until it is finally dismissed.

"ARTICLE VII—INTERSTATE COMMERCE COMMISSION

"SEC. 740. If, in any application filed with the Commission pursuant to section 20a of the Interstate Commerce Act for authority to issue or modify securities, the applicant shall allege that the purpose in making such application is to enable it to file a petition under the provisions of this chapter, the Commission shall take final action on such application as promptly as possible, and in any event within one hundred and twenty days after the filing of such application, unless the Commission finds that a longer time, not exceeding sixty days is needed in the public interest.

"ARTICLE VIII—FINAL DECREE AND REVIEW

"SEC. 745. Any final order or decree of the special court may be reviewed by the Supreme Court of the United States upon application for certiorari made by any person affected by the plan who deems himself aggrieved within sixty days after the entry of such order or decree, pursuant to the provisions of the Federal Judicial Code.

"SEC. 746. In the decree approving and confirming the plan the court may require such reports of the action taken by the petitioner thereunder in the execution of the plan as may be necessary to a final disposition of the cause, and in its final decree disposing of the cause the court shall retain jurisdiction in the district court to the extent necessary to protect and enforce the rights of the parties under said plan and the orders of the court thereon.

"ARTICLE IX—FILING RECORD WITH COMMISSION

"SEC. 750. The clerk of the court in which any proceedings under this chapter are pending, shall forthwith transmit to the Interstate Commerce Commission copies of all pleadings, petitions, motions, applications, orders, judgments, decrees and other papers in such proceedings filed with the court or entered therein, including copies of any transcripts of testimony, hearings or other proceedings that may be transcribed and filed in such proceedings together with copies of all exhibits, except to the extent that the court finds that compliance with this section would be impracticable.

"ARTICLE X—TERMINATION OF JURISDICTION

"SEC. 755. The jurisdiction conferred upon any court by this chapter shall not be exercised by such court after July 31, 1940, except in respect of any proceeding initiated by filing a petition under section 710 hereof on or before July 31, 1940."

Approved, July 28, 1939, 9:45 a. m., E. S. T.

FILED
JAN 14 1949
CHARLES ELMORE

IN THE

Supreme Court of the United States

October Term, 1948

No. 511

IN THE MATTER OF
THE PEORIA AND EASTERN RAILWAY COMPANY

INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY,

Petitioners,

v.

THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

SUPPLEMENT I TO PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

CHARLES S. ARONSTAM,
ARTHUR A. BALLANTINE,
JOHN M. HARLAN,
Counsel for Petitioners.

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FINAL DECREE—November 16, 1948 (R. 39)

Endorsed: U. S. District Court
Filed Nov. 16, 1948
S. D. of N. Y.

IN THE
DISTRICT COURT OF THE UNITED STATES
For the Southern District of New York

In the Matter of The Peoria and Eastern Railway Company, Petitioner.	In Proceedings for a Railroad Adjustment. No. 76016

In this final decree the following terms shall have the indicated meanings:

(a) New York Central—The New York Central Railroad Company.

(b) Big Four—The Cleveland, Cincinnati, Chicago and St. Louis Railway Company.

(c) Operating Companies—The New York Central and the Big Four.

(d) Peoria and Eastern—The Peoria and Eastern Railway Company.

(e) Income Bonds—The Income Mortgage Bonds of the Peoria and Eastern dated February 22, 1890, maturing April 1, 1990, in an aggregate principal amount not in excess of $4,000,000.

(f) Operating Agreement—The agreement dated February 22, 1890 and the supplement thereto of the same date between the Big Four and the Peoria and Eastern, pursuant to which the property of the Peoria and Eastern has been operated since 1890.

The Peoria and Eastern having on or about March 29, 1940 filed its petition praying that this Court be constituted under Section 710, Chapter XV of the Bankruptcy Act (53 Stat. 1134) and praying for an adjustment of its maturing debts under the said Chapter XV of the Bankruptcy Act; and

This Court having approved a plan of adjustment by its Final Decree, dated July 23, 1940, as amended by order supplemental to decree dated April 3, 1941, and having provided in Section 24 thereof:

> "Section 24. All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', *upon objection by the representative of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so.*";

and

The New York Central having proposed at the meeting of the Board of Directors of the Peoria and Eastern held February 24, 1943, to apply the net earnings for the year 1942 against the balance of the inter-company accounts in favor of the New York Central and Big Four, and the director of the Peoria and Eastern representing the Income Bondholders having objected to the crediting of such net earnings to the Operating Companies; and

The balance of the inter-company accounts in favor of the New York Central and Big Four as shown upon the books of the Peoria and Eastern being, as of December 31, 1942, $2,356,687.33 and, as of December 31, 1945, $2,600,-441.68; and

The sum of $1,579,162.32, representing net earnings of the Peoria and Eastern for the years 1942, 1943 and 1944 having been held in a special account in the Central Hanover Bank and Trust Company pending the determination of this proceeding,

Now this cause having come on to be further heard:

1. Upon the petition of the New York Central and the Big Four dated April 1, 1943, praying for the appointment of a Special Master to hear and report to this Court his findings and conclusions as to the amount and validity of the inter-company accounts between the New York Central and Big Four and the Peoria and Eastern, as referred to in Section 24 of the decree, as amended, to the intent that said inter-company accounts may be settled and stated by this Court, and the right of the New York Central and the Big Four to have said earnings applied in reduction of the indebtedness of Peoria and Eastern to them as shown

by said inter-company accounts, as so settled and stated, proved and established, and following the statement of such accounts that such modification be made in Section 24 of said decree, as amended, as may be just and proper in the premises;

2. Upon the order of this Court, dated May 21, 1943, appointing Francis H. Horan, Esq., as Special Master to hear and report on the amount and validity of the inter-company accounts between the New York Central and the Big Four, and the Peoria and Eastern, and appointing Charles S. Aronstam, Esq., as counsel to represent the Income Bondholders of the Peoria and Eastern in the proceedings before the Special Master;

3. Upon the petition of the Peoria and Eastern, dated June 24, 1943, for approval of the appointment of F. W. H. Adams, Esq., as counsel to represent it in the accounting proceeding before the Special Master, and upon the Order of this Court, dated July 2, 1943, granting the said petition;

4. Upon the testimony of witnesses adduced and the exhibits presented before the Special Master;

5. Upon the report of the Special Master, filed April 28, 1947;

6. Upon the objections of the New York Central and the Big Four, of the Peoria and Eastern, and of the Income Bondholders of the Peoria and Eastern to the report of the Special Master;

7. Upon the arguments and briefs of counsel and upon the opinion of this Court, dated April 24, 1948;

8. Upon the petition of the Income Bondholders for re-argument of a limited phase of the case and this Court's order, dated June 4, 1948, based upon its opinion, dated May 31, 1948, denying such petition; and

9. Upon the stipulation of the parties, dated October 15, 1948, with respect to "Superimposition" and "Grain Transited at Indianapolis and Reshipped to Chicago" as those terms are defined in the opinion of this Court, dated April 24, 1948; and

10. Upon all the other proceedings heretofore had herein,

This Court hereby ORDERS, ADJUDGES and DECREES as follows:

Sec. 1—(a) The amount and validity of the inter-company accounts between the Big Four and New York Central and the Peoria and Eastern be, and the same hereby are, settled and stated as of December 31, 1945, in the amount of $1,266,008.20 in favor of the New York Central and against the Peoria and Eastern and in the amount of $1,158,173.12, in favor of the Big Four and against the Peoria and Eastern, including interest to December 31, 1945.

(b) The New York Central and the Big Four having proved and established their right to withdraw net earnings of the Peoria and Eastern by way of recoupment and repayment of said inter-company accounts, and the amount of $1,579,162.32, representing net earnings of the Peoria and Eastern for the years 1942, 1943 and 1944 being held in a special account in the Central Hanover Bank and Trust

Company, the New York Central and the Big Four shall withdraw said amount and credit the same against the inter-company accounts as of the date of this decree, and the New York Central is authorized and empowered to apply any further net earnings of any succeeding year in recoupment and repayment of said inter-company accounts during the term of the Operating Agreement.

Sec. 2—The inter-company accounts as hereby settled and stated, include and give effect to adjustments and corrections in said accounts in favor of the Peoria and Eastern and against the New York Central and the Big Four as follows:

(1) In confirmation of the Special Master's report:

(a) $91,639.43 for charges made by the Operating Companies in connection with Pullman service on the lines of the Peoria and Eastern which charges are hereby disallowed as follows:

	Principal	Interest to December 31, 1945
For the year 1936	$11,062.31	$4,646.17
" 1937	12,055.13	5,063.15
" 1938	10,590.25	3,812.49
" 1939	13,423.99	4,027.19
" 1940	12,967.85	3,112.28
" 1941	4,279.86	1,350.00
" 1942	5,031.41	217.35

(b) $1,494.97 for overcharges made in connection with sale of used New York Central equipment to the Peoria and Eastern which amount is hereby disallowed and credited in the inter-company accounts to the Peoria and Eastern as follows:

	Principal	Interest to December 31, 1945
for two locomotives in 1940	$1,149.98	$344.99

(c) $8,203.00 for under-charges in the sale of used Peoria and Eastern equipment to the New York Central which amount is hereby credited in the inter-company accounts to the Peoria and Eastern as follows:

	Principal	Interest to December 31, 1945
for three baggage cars in 1940	$6,310.00	$1,893.00

(2) In modification of the Special Master's report:

(a) $55,610.74 in connection with maintenance of traffic offices at Pittsburgh, Indianapolis, Peoria, and Minneapolis, which amount is hereby disallowed and credited to the Peoria and Eastern in the inter-company accounts as follows:

Year	Principal	Interest to December 31, 1945
1933	$9,179.86	$6,609.50
1934	20,869.86	13,774.11
1935	3,235.88	1,941.53

(b) The New York Central shall reverse the charge against the Peoria and Eastern in the amount of $19,312.22 made in 1945 with respect to expenses allocated incident to the reciprocal use of tracks belonging to the New York Central and the Peoria and Eastern in the Indianapolis Terminal area during the years 1936-1945, based upon a trackage study made in 1923.

Sec. 3—The above changes in the inter-company accounts are summarized as follows:

(1) Advances by New York Central and Big Four as of December 31, 1945, as shown on books of the Peoria and Eastern			$2,600,441.68
Adjustments by this decree			
	Principal	Interest	
Pullman operations (Section 2, par. 1, a)	$ 69,410.80	$22,228.63	
Overcharges on sale of used equipment (Section 2, par. 1, b)	1,149.98	344.99	
Under-charges on sale of used equipment (Section 2, par. 1, c)	6,310.00	1,893.00	
Disallowance of cost of traffic offices (Section 2, par. 2, a)	33,285.60	22,325.14	
Disallowance of reciprocal trackage expense (Section 2, par. 2, b)	19,312.22		
Net decrease	$129,468.60	$46,791.76	176,260.36
Corrected advances			$2,424,181.32

Sec. 4—Any amount of interest charged against the Peoria and Eastern on account of the above stated principal adjustments for any period subsequent to December 31, 1945 shall be credited to the Peoria and Eastern as of the date of this decree.

Sec. 5—The stipulation of the parties dated October 15, 1948 is approved, and in accordance with such stipulation no change is made in the freight revenue accounts of the Peoria and Eastern.

Sec. 6—The charges against Peoria and Eastern freight revenues reported in the accounts for the year 1945 in the amount of $798,706.75 representing "government cutbacks" for the years 1941 to 1945 inclusive, should have been distributed over the accounts for the years 1941-1945. However, since the inter-company accounts as herein adjusted will produce no surplus in any year available for payment of interest on income bonds and distribution of this charge will have no effect on the settled and stated balance of accounts as of December 31, 1945, such distribution shall not be made. But, since distribution of this charge over the years 1941-1945 would have resulted in the Peoria and Eastern's having had no loss for the year 1945, any amount of interest charged against the Peoria and Eastern for any period subsequent to December 31, 1945 on account of the reported deficit in the year 1945 shall be credited to the Peoria and Eastern as of the date of this decree.

Sec. 7—(a) Nothing in this decree or in this proceeding shall determine the rights of the parties, upon the termination of the Operating Agreement, with respect to the destruction of the Moorefield Terminal and such rights shall be left open for future determination.

(b) This Court lacks jurisdiction to decide the "Indianapolis Trackage" dispute, as defined in part XIII of the opinion of this Court, dated April 24, 1948, and the "Peoria and Pekin Switching Charges" dispute, as defined

in part XVI of the opinion of this Court, dated April 24, 1948, there having been no prior recourse as to either to the Interstate Commerce Commission.

Sec. 8—All objections of the Income Bondholders, of the Peoria and Eastern and of the New York Central and the Big Four to the report of the Special Master are denied except as they are specifically granted by the terms of this amendment to the decree of this Court, dated July 23, 1940, as amended April 3, 1941.

Sec. 9—The Court hereby reserves full jurisdiction to consider and approve, and authorize or disapprove, after hearing, upon due notice, expenses of every kind not herein approved or authorized.

Sec. 10—This Court hereby reserves full jurisdiction to correct or perfect this decree, to take any other or further action in aid of this decree and otherwise to take all such supplementary action as this Court may deem proper in the premises; provided, however, that no action taken pursuant to this Section shall impose, or result in, any liability on anyone for or in respect of any action theretofore taken in accordance with this decree.

Dated: November 16, 1948.

LEARNED HAND,
United States Circuit Judge.

ALFRED C. COXE,
United States District Judge.

CARROLL C. HINCKS,
United States District Judge.

OPINION—April 24, 1948 (R. 33)

UNITED STATES DISTRICT COURT

FOR THE SOUTHERN DISTRICT OF NEW YORK

WILLIAM C. EWEN, et al.,

Claimants,

v.

PEORIA & EASTERN RAILWAY COMPANY,

Defendant.

Before:

L. HAND, COXE and HINCKS, JJ.

Upon objections to the report of a special master, auditing accounts between the Peoria & Eastern Railway Company, the defendant, and the Cleveland, Cincinnati, Chicago & St. Louis Railway Company and the New York Central Railroad,* under a decree of this court of July 29, 1940, as amended on April 29, 1941.

JOHN M. HARLAN, CHARLES S. ARONSTAM, ARCHIE S. KARP, LYMAN M. TONDEL, JR., and WILLIAM B. SHEDD, for the Income Bondholders.

GERALD E. DWYER and SAMUEL H. HELLENBRAND, for the "Central."

F. W. H. ADAMS and PETER KEBER, for the "Peoria."

* For convenience, when we have occasion to speak of the Cleveland, Cincinnati, Chicago & St. Louis Railway Company before its union with the New York Central Railroad in 1930 or of the two jointly thereafter we use the name, "Central"; and for the Peoria & Eastern Railway Company, the name, "Peoria."

Opinion—April 24, 1948

L. HAND, C. J.: This case has now come back to us upon objections to the report of the Master under the rules.* On July 29, 1940, we passed a decree, Section 24 of which, as amended by our opinion on April 3, 1941, we quote in the margin.** Early in 1943 the "Central" filed the annual account between the roads required by Article Fourth of the Operating Agreement, to which the director of the "Peoria" who had been appointed by the Bondholders filed objections. Thereafter and on April 1, 1943, the "Central" petitioned for a supplemental order, appointing a master under this decree to hear and report upon the validity and amount of their claim against the "Peoria" in the sum of $2,485,482.58, as of December 31, 1939; and by order entered May 20, 1943, we appointed a master to conduct such an inquiry. The parties to the accounting were the "Central," a protective committee of the Income Mortgage Bondholders, and the "Peoria." On July 2, 1943, we appointed an independent attorney to represent the "Peoria" upon a petition of the "Central" with the understanding that he should "to the best of his ability as an attorney, protect the interest of the Peoria & Eastern * * * and * * * look only to

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* Rule 53(e)(2).

** "Section 24. All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', upon objection by the representatives of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so."

the best interest of the Peoria & Eastern without regard to any * * * control," by the "Central." The Bondholders engaged a firm of accountants who were given access to the books of the "Peoria" and of the "Central," and who reported to them on June 30, 1944. This report the "Central" took some six months to prepare to meet, and the hearings began on February 2, 1945. The Master took some four thousand pages of testimony, considered nearly six hundred exhibits, and filed his report on April 28, 1947. The original claim of the "Central" had grown by the end of 1945 to $2,600,441.68; but the account as stated by the Bondholders showed not only that no part of this was due, but that there was due to the "Peoria" over $12,000,000. By consent, neither party made any effort to carry the accounting back of January 1, 1920; but the Bondholders challenge the accounts for every year thereafter until the close of the year 1945. Before taking up the several items which make up their challenge, it is necessary to consider (1) the underlying relations between the "Central" and the "Peoria" which determined their mutual rights and duties; (2) the effect of the annual statements of account of the "Central" made to the "Peoria" and to the trustees for the Bondholders; and (3) the Statute of Limitations. Throughout we shall assume an acquaintance with our earlier decisions*; but we will endeavor in our discussion to state of the separate items enough of the facts to make understandable what we say.

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* *Ewen* v. *Peoria & Eastern Railway Company*, 34 Fed. Supp. 332; 37 Fed. Supp. 917.

I.

The Duty of the "Central" to the "Peoria," and The Burden of Proof.

As we said in our original opinion, the "Central" completely dominated the "Peoria" through the ownership of a majority of its shares, and the first question is, how far as a majority shareholder, it was free to use its power over the minority and the Bondholders to its own advantage; in short, to what extent it occupied the conventional position of a fiduciary. As the Bondholders point out, the Court of Appeals of New York in *Farmers Loan & Trust Company* v. *New York & Northern Railway Company** and *Ticonderoga Railroad Company* v. *Delaware & Hudson Company*† was concerned with the duties imposed upon one railroad as majority shareholder of another; but we cannot find in either decision any guidance in construing the agreement of February 22, 1890, under which the "Peoria" was operated throughout the period before us. We shall assume that, as its majority shareholder, the "Central" would have been subject to the usual limitations of a trustee in any dealings between the two, had it not been for the powers granted it in the "Agreement"; but both the Bondholders and the "Peoria" concede that these to some extent modified its duty. A moment's reflection shows that if it were to be held strictly accountable as a fiduciary in the conventional sense, the "Agreement" could not have been performed at all. Both parties entered into it, because, as it recites, they thought that it would be "beneficial to the

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* 150 N. Y. 410.
† 204 N. Y. 288.

business and traffic of said railways that the same be put under one management"; and "one management" presupposed that the "Central" should have power to determine the interests of both in those mutual transactions which would constantly arise between the two. Moreover, it was apparent that those determinations could not be "beneficial" at once to the "business and traffic" of the "Central" and of the "Peoria," unless the "Central" were permitted to profit from the joint "business and traffic." Indeed there would have been no conceivable motive for its entering into the agreement at all, if it were bound to fix the terms of every transaction with an eye only to the interest of the "Peoria."

The law has dealt with situations in which it is understood that an agent or a trustee is to deal with his principal or beneficiary in the interest of both; and the usual solution has been to say that the fiduciary must be "fair" to the beneficiary.* In *International Radio Tel. Co.* v. *Atlantic Communications Co.*,** the Circuit Court of Appeals for the Second Circuit accepted as a test: "whether the proposition submitted would have commended itself to an independent corporation"; and that is very close to what seems to us to be the proper test, although it needs further analysis. Whatever the right rule, clearly it does not advance to a solution to say that the fiduciary must be "fair," or must not "abuse" his power, or that he shall use it as the parties "intend." Here, as so often, a court must "interpret" the words, by imputing to them that meaning which in the main it will gather from the dominant purpose of the

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* *Restatement of Agency*, §392; *Restatement of Trusts*, §216-(2)(e).

** 290 Fed. Rep. 698, 702.

document as a whole. When the "Central" and the "Peoria" declared their wish that both should "be put under one management," they could only have meant that the "Peoria" should be treated as though it were a division of the "Central," so far as concerned the routing of traffic, the upkeep, disposition and distribution of rolling stock, the maintenance of repair shops, engine-houses and other buildings. In short, the "Peoria" was to become part of a single railway system, operated as a constituent unit after the conventional pattern in such cases. There were advantages and disadvantages in this, the prospective balance between which seemed inducement enough to both. Implied was a duty of the "Central" not to discriminate against the "Peoria" by denying it that share of traffic which it would allocate to a wholly owned division; and implied on the other side was a surrender by the "Peoria" of any right to ask more; so much and no more was to be the general frame of their mutual relations. That does not, however, give any clue to what part of the income and of the expenses of the new system should be assigned to the "Peoria," and this is the source of most of the difficulties, because the "Peoria" did not, and could not, appear as an independent party in any of the transactions of the "Central" with third persons. The proper apportionment inevitably presupposed some hypothetical and fictitious dealings between the two, determined by the "Central" in the interest of both; and it is necessary first to decide what, if any, general principle should govern these.

Theoretically, the ideal principle, if only it were in practice capable of application, would be that the "Central" should not use its power to the prejudice of the "Peoria": that is, that it should fix the terms of any transactions be-

tween the two as though each had in fact exerted its bargaining power against the other at arm's length. Indeed, there are situations in which that can be done within a narrow margin of error. For example, an agent permitted to trade with his principal in fungibles, dealt in upon an active market, can fix with substantial accuracy the price at which the principal would buy or sell, if the two dealt at arm's length. In the case at bar, however, it must be at once admitted that in the transactions here involved, it is wholly impossible even approximately to set the terms upon which the "Central" and the "Peoria" would have agreed at arm's length. On the other hand it may in fact be possible, to set limits on either side outside of which one can say with some assurance that the parties would not have agreed at all: that is to say, that the "Peoria" would have been unwilling to accept less and would—with possible recourse to the Interstate Commerce Commission —have been successful in its refusal; and that the "Central" on the other hand would have been unwilling to give more. In other words, although it is impossible to know whether the "Central" did discharge its duty, as fiduciary, to divide the income and expenses as they would have been divided, had it and the "Peoria" traded it out against each other, it may be possible to learn whether the actual division was worse than the "Peoria" would have accepted, or could have been forced to accept. Under such a test the crucial question becomes who carries the burden of proof. If the "Peoria" carries it, it will not succeed as to a given division, unless it was outside the range we have described; if the "Central" carries it, it will not succeed unless it would have refused to deal at all on terms more favorable to the "Peoria" than those it made. De-

cisions such as *Geddes* v. *Anaconda Mining Company*,* and *Pepper* v. *Litton*** are quite beside the point; they dealt with occasions upon which the fiduciary—a director, or a majority shareholder—had not been authorized to deal with his principal. On the other hand, although we have not been able to find any cases which have explicitly laid down that the burden of proof is on the beneficiary, there are several in which the result appears to have depended upon just that.† They were situations in which the charter permitted the directors to deal with the company; and in each the beneficiary failed because he had not affirmatively proved that the fiduciary had been "unfair." On this branch of the case we therefore conclude that the effect of the "Agreement" was as follows. As to the actual conduct of the business—the routing of traffic, the disposition and acquisition of plant or rolling stock, the locating of cars and all other matters of joint "management"—the "Peoria" and the Bondholders have the burden of proof to show that the "Central" managed the "Peoria" as it would not have managed a wholly-owned division of its system. As to the division of the income and expenses, the "Peoria" and the Bondholders have the burden of proof to show that, had the two roads been dealing at arm's length, the "Peoria" would not have accepted the division made. In applying this second test, it must always be assumed that management as a single system over which the "Central" has control is not to be embarrassed.

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* 254 U. S. 590.

** 308 U. S. 295.

† *Goldboss* v. *Reimann*, 55 Fed. Supp. 811 (S. D. N. Y.), aff'd on opinion below, 143 Fed. (2) 594 (C. C. A. 2); *Speigel* v. *Beacon Participations*, 297 Mass. 398; *Everett* v. *Phillips*, 288 N. Y. 227; *Helfman* v. *American Light & Traction Co.*, 121 N. J. Eq. 1.

II.

Accounts Stated.

The "Central" insists that the Bondholders are concluded from challenging the accounts which were annually submitted by the "Central" to the "Peoria," and by both the "Central" and the "Peoria" submitted to the trustees for the Bondholders. At the end of each year, in accordance with Article Fourth of the "Agreement," which we quote in the margin,* the "Central" made up an account of the transactions between itself and the "Peoria," and submitted it to the trustees for the Bondholders and to the directors of the "Peoria"; and the directors in each case passed a resolution approving the account as rendered. The "Peoria" also submitted the accounts to the mortgage trustees of the Bondholders, who retained them without objection, though they did not formally approve them. Article Sixth of the mortgage of the "Peoria" provided, among other things, that on or before the first day of March of each year the "Peoria" should furnish the trustees with a statement of earnings and income; and, "If the trustees shall not be satisfied with said statement, or if said trustees shall be notified in writing by the holders

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* "Fourth.—Within sixty days after the 31st of December, 1890, and each year thereafter, the Cleveland Co. is to make up and state all its receipts for earnings and income from the said lines of railroad operated by it under these presents, and from said purchase money lien, and all its disbursements for interest or rental as aforesaid, and for the cost and expense of using, operating and maintaining said lines of railroad and of complying with the requirements of these presents, and to render proper accounts thereof to the Peoria Co. and to the trustees of its said second mortgage as in said second mortgage required."

of bonds to the amount of one-fifth of the amount outstanding that they object to the same within thirty days after the same shall have been received by the trustees, it shall be the duty of the said trustees forthwith to notify the Railway Company of such objection." The trustees had the right to inspect the books of the "Peoria" by an expert accountant, for whose services the "Peoria" would pay; and then the Article went on: "If the said difference for any reason shall not be adjusted by agreement * * * it shall be lawful for and the duty of the trustees to file a bill in equity against the Railway Company in any court of competent jurisdiction, for an account of the net earnings and income under the provisions of this mortgage, and if it shall be adjudged in such action that there are such net earnings and income available * * * then, unless the Railway Company shall, within three months after such adjudication, pay the said balance * * * such non-payment shall constitute a default in the payment of interest, for which the trustees shall be authorized to proceed under the terms of the second, third and fourth articles of this mortgage. The remedy herein provided for ascertaining the amount of the net earnings, in case of dispute, shall be exclusive of all other proceedings, actions, suits, and demands whatsoever." The Fourth Article of the mortgage provided that "No delay or omission of the trustees or of the holders of the bonds hereby secured to exercise any of the rights and powers given to them * * * by these presents, shall be held to impair or defeat said rights and powers, or any of them, or be construed or taken to be a waiver of them, or of any of them, or an acquiescence in any default upon which the same may arise."

Had the "Peoria" not been under the control of the "Central" there could have been no question that the annual rendition of these accounts and the express approval of them by the directors' resolution, would have made them accounts stated, and have concluded the "Peoria" unless it could have opened them for mistake or fraud, of which there was neither. The Bondholders answer that, since the "Peoria" was under the "domination" of the "Central," the assent of its directors was no assent at all, and that the accounts remained merely accounts rendered. That is quite untrue. The directors were the authorized representatives of the "Peoria," and there is not a tittle of evidence that they did not honestly do their duty as they understood it: that is, that they did not examine the accounts and in fact approve them. What is, however, true is that, because of their equivocal position, as directors elected by and under the "domination" of the "Central," their assent did not conclude the "Peoria" or the Bondholders, if either chose to challenge their action. The critical fact is that until they did, and unless they did, the accounts stood as accounts stated quite as though the "Central" had not "dominated" the "Peoria," and from that it follows that whatever conduct or inaction disabled either the "Peoria," or the Bondholders, from making their challenge left the accounts as accounts stated. In short, the directors' consent, though voidable, was not void. There cannot be any doubt that the Bondholders did disable themselves from making such a challenge. Their trustees had received the accounts from both the "Peoria" and the "Central" and had retained them without objection, which was quite as conclusive an assent as the formal resolutions

of the directors.* Moreover, this is the just result, plainly forecast in the mortgage, whose draftsmen were aware that just such disputes as have now arisen might arise, and who wished to prevent their settlement being put off until the evidence, then accessible, might have disappeared. For that reason they provided the Bondholders with full opportunity of acquainting themselves with how the "Central" was discharging its duties, and gave them ample remedy for any derelictions they might discover. Moreover, this remedy was made exclusive so that the "Central" might be able to know as it went along whether it might safely continue the joint "management" in the way it had been conducting it.

The Bondholders retort that the language, which we have quoted from Article Fourth of the mortgage, protected them against their own inaction or that of their trustees; and that consequently the continued absence of objection by either was without significance or legal effect. We do not agree. The provision of Article Fourth which preserved the "rights and powers * * * given by these presents," irrespective of inaction by the trustees or the Bondholders, was intended to apply only to rights conditioned upon a defined default, and not to incidents of the exclusive remedy provided by Article Sixth for the ascertainment of net earnings and income. This construction is suggested

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* *Oil Company* v. *Van Etten*, 107 U. S. 325, 333, 334; *Bonwit Teller & Co.* v. *United States*, 283 U. S. 258, 265; *Daube* v. *United States*, 289 U. S. 367, 370; *Boise* v. *Talcott*, 264 Fed. Rep. 61, 66 (C. C. A. 2); *Leathe* v. *Title Guaranty Trust Co.*, 18 Fed. (2) 41, 49 (C. C. A. 8); *Kretni Development Co.* v. *Consolidated Oil Co.*, 74 Fed. (2) 497, 500 (C. C. A. 10); *Restatement of Contracts*, §422(2); *Williston on Contracts*, §1863.

both by the context and content of the very clause upon which the Bondholders rely. Article Fourth, in which it occurs, confirms to the trustees and the Bondholders' rights relating to a receivership and sale of the mortgaged property; rights which by their very nature could not come into effect until after a default. Indeed, under Article First the "Peoria" as mortgagor was entitled to remain in possession until default. Again, by the very language of the clause in question the draftsman indicated his concern lest a failure to exercise their rights might be deemed "an acquiescence in any default upon which the same" (the rights) "may arise": language, plainly directed to rights dependent upon a default. Article Sixth makes it plain that the "right" to object to the annual statements of accounts—and in case of dispute to sue for an accounting—cannot constitute a "default" until entry of a judgment declaring that income additional to that originally reported is available for bond interest, and until that judgment remains unpaid for three months. Only after such a "default" are the trustees empowered to proceed under Articles Second, Third and Fourth. Articles Second and Third are expressly confined to rights arising upon default, and the fact that Article Sixth places Article Fourth in the same category tends to support this construction. Furthermore, we find some significance in the verbal distinction between the "rights and powers," which Article Fourth was solicitous to preserve, and the "remedy • • • for ascertaining the amount of the net earnings," which Article Sixth made "exclusively of all other proceedings." This distinction may possibly also explain a curious difference between the several provisions for the Bondholders'

control over their trustees. Under Article Sixth, the holders of only one-fifth of the bonds may initiate the "remedy" for ascertaining the net earnings; but to compel the exercise of a "right" upon a default under Article Second, the holders of one-quarter of the bonds are required. However that may be, we think it plain that the "remedy" here referred to included the procedure expressly stated in Article Sixth "for ascertaining the amount of the net earnings, in case of dispute" as well, of course, as all incidental procedural steps to that end: not until that "remedy" resulted in a judgment, followed by a "default," did the "rights and powers" referred to in Article Fourth arise.

The Bondholders seek to escape the effect of these provisions by saying that, although they may have lost their rights as lienors on the income, they retained them as unsecured creditors of the "Peoria"; and that, if the "Peoria" be entitled to challenge the accounts, they are entitled to their share in any funds which may come into its treasury. One answer to this is that the "Central" was itself to render the accounts to the Bondholders' trustees, whose assent made them accounts stated as between the Bondholders and itself, as much as between the "Peoria" and itself. Another answer is that it would be altogether unreasonable to confine the effect of Article Sixth to the interests of the Bondholders as lienors, for that would accomplish nothing but to deprive them of their priority over other creditors of the "Peoria." That might have been a plausible purpose—though it would not have been convincing—if there could have been other unsecured creditors; but there could not, for the "management" was

to be in the hands of the "Central," and the "Central" undertook to pay, not only fixed charges and taxes, but "all claims arising out of the operation or management thereof." Thus, if, in spite of the loss of their rights as lienors, the Bondholders remained unsecured creditors to the extent of any income which the "Central" failed to pay, they would have been the only creditors, and the only difference in their rights would be that they must proceed by execution rather than by foreclosure. For the foregoing reasons we hold that, as to all questions which affected the income or expenses of the "Peoria," the accounts became accounts stated as against the Bondholders by their failure seasonably to object. The first objection made to the accounts was on February 24, 1943, and, as we have said, by the Bondholders' director; hence the Bondholders are concluded as to all net income which accrued before January 1, 1942.

The "Peoria" is not so concluded, because the minority shareholders never assented to the correctness of the accounts, and the directors' assent was always open to challenge by them. It is true that they have never questioned the action of their directors, and that we have done what we could to protect them by appointing an able, assiduous and disinterested attorney for the "Peoria." Nevertheless we should be unwilling to deny them the benefit of any rulings which we make in favor of the Bondholders during the years in which the accounts are open to the Bondholders themselves, or, so far as the minority are not concluded by the Statute of Limitations, even to deny them the benefit of the same rulings back of those years. This position raises an added problem, however, in those years in which the

Bondholders are concluded by the accounts stated. Should the fact that they lost the right to surcharge the accounts inure to the benefit of the "Peoria," (i.e. the minority shareholders), or to that of the "Central"? In other words, in computing the earnings properly due to the "Peoria" should the "Central" be allowed a credit in each of those years up to $160,000—four per cent upon the principal of the mortgage? Article Third of the "Agreement" is the only relevant provision: the "Central" is to "receive all earnings and income" of the "Peoria" and to "apply the net earnings" first to the payment of the fixed charges, to "apply the balance * * * to the payment of interest" on the mortgage, "and pay over to the Peoria Co. any amount thereof finally remaining." That is a direction to the "Central" how to dispose of the income; and, if the Bondholders had surrendered, once and for all and in advance, a share of their right to the income—say, a fifth—it may well be that in subsequent years the "Central" would have had to distribute to the "Peoria" what was left after they had distributed four-fifths to the Bondholders. That is not what took place. In each year before 1942 the Bondholders became at once entitled to any income beyond that disclosed in the accounts up to $160,000 before anything was to go to the "Peoria"; and that right remained unimpaired throughout that year. It was only in the subsequent year that they lost it by assenting to the correctness of the accounts; the result was not different from a formal release of the claim that had accrued against the "Central" in their favor. We cannot see why this should be treated as an assignment to the "Peoria"; nor do we discover any equity which requires the "Central" to pay to the minority shareholders sums

which the "Agreement" did not intend them to have. The equities being equal, we are content to let the legal right prevail, and we hold that, before the "Peoria" becomes entitled to share in the income of any year before 1942, it must concede a debit up to the $160,000 which would have gone to the Bondholders.

III.

The Statute of Limitations.

The disposition we have made of the defense of accounts stated makes it unnecessary to consider the Statute of Limitations as applied to the Bondholders. True, their trustees never objected to the accounts at any time, but we accept as an equivalent the objection on February 24, 1943, of the Bondholders' director. Since, even so, the accounting cannot go back of January 1, 1942, no question of limitation arises. Not so as to the "Peoria," whose rights it may assert on behalf of the minority. The relevant statute is that of New York,* and the action would be against the "Central" upon the breach of their duty to account in accordance with Article Fourth of the "Agreement." We will assume for argument that an action brought against the "Central" on an open account would require the accounting to go back to the first transactions

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* *Hargadine-McKittrick Dry Goods Co.* v. *Hudson,* 122 Fed. 232, 234 (C. C. A. 8); *In re German-American Improvement Company,* 3 Fed. (2) 572, 575 (C. C. A. 2); *In re Povill,* 105 Fed. (2) 157 (C. C. A. 2); *Biggs* v. *Mays,* 125 Fed. (2) 693, 698 (C. C. A. 83; *In re Resler,* 95 Fed. 804 (D. Minn.); *In re Stoddard Bros. Lumber Co.,* 169 Fed. 190, 194 (D. Idaho); *In re Strotz,* 50 Fed. Supp. 322, 325 (S. D. Cal.).

between the parties; that is, to 1920.* However, for the reasons we have already given, it would be wrong to treat an action brought in the "Peoria's" name, as merely an action upon an open account; it would not become such until the assent of the "Peoria's" directors to the correctness of the accounts was set aside. Even though we assume, as we do, that the "Peoria" may speak in the name of its minority shareholders, it must do so subject to those conditions which would have limited a shareholders' derivative suit brought in the "Peoria's" name to set aside the assent. One of those conditions would be the Statute of Limitations, the period of which the New York statute fixes at ten years in suits which, like this, must be brought in equity.** As we have just said, the first objection to the accounts—except for one that was later settled—was by the Bondholders' director on February 24, 1943; and that objection did not extend to the accounts for earlier years. Nevertheless, on April 1, 1943, the "Central" petitioned to be allowed to withdraw surplus income in payment of their advances, and this opened the accounts for the whole period save as they were foreclosed as accounts stated. We cannot find in the record when for the first time in the proceeding so instituted the "Peoria" explicitly challenged the accounts stated, but we assume that it was some time during 1943. Since it must have been after April 1st of that year, it was more than ten years after the account became an account stated for the year 1932. Hence it follows that the "Peoria" may insist upon a restatement of the accounts for

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* *New York Civil Practice Act*, §56.

** *New York Civil Practice* Act, §53; *Potter* v. *Walker*, 276 N. Y. 15, 25, 26.

1933 and those which followed, so far as the accounts rendered were open to challenge on the merits.

This concludes our preliminary rulings, and we proceed to the specific items of surcharge.

IV.

Freight Revenues.

The first of these items is that the "Central" did not divide the freight revenues "fairly": it is in three parts, called respectively "Superimposition," "Minimums" and "Equalization." It was the general practice in the territory of the Central Freight Association to divide joint rates between two or more carriers, in proportion to the distance over which each hauled a shipment. That applied without qualification in the case of what is known as an "overhead" carrier: i.e. one which hauls a shipment intermediately between the first or "originating" carrier and the last or "terminating" carrier. A division of the joint rate in proportion to the miles of each carrier's haul does not, however, make allowances for the cost of loading, switching, making up the train at the point of origin, or of the costs of discharge at the point of unloading. To meet these it has been long customary to compute the haul of a shipment by adding what is called "inflated mileage" at each end of the haul, and credit the "originating" and the "terminating" carrier with the addition. This is done by dividing the joint mileage into sections or "blocks," fixed by the consent of the carriers concerned. For example, if a shipment starts on Road A, passes over the rails of Roads B and C and ends on Road D, the distance

which it has travelled on A and D will be divided into sections or blocks which we may call X, Y and Z, of Road A, and U, V and W, of Road D. No matter where on any block of Road A the shipment starts or ends, and no matter where on any block of Road D it ends or starts, the joint rate will be divided upon the assumption that Road A has hauled it over the whole of block X, or Y, or Z on which it has started or ended, and similarly as to Road D. True, neither Road A nor Road D will receive any return for the costs of loading or discharge, when a shipment begins to move, or comes to a stop, at the further end of a block; but as to all shipments beginning or ending in the middle of a block, it will receive a proportion of the rate increased by the number of miles of that block over which the shipment has not been hauled. By and large this is designed to make up for the extra costs of all shipments "originating" or "terminating" on that block.

It often happens, however, that this allowance is not enough. Sometimes the proportion of a joint rate, which an "originating" or a "terminating" carrier will receive —even though it hauls over two blocks—will not pay it for its added costs at the beginning or end of its haul. In such cases it is the common, though not the uniform, practise to make an arbitrary allowance of twenty per cent of the joint rate to each "originating" or "terminating" carrier, if its proportion of the rate, calculated upon the end block together with any intervening blocks does not come to that much. This allowance is called a "minimum."

The "Peoria" does not join in the Bondholders' claims because its attorney does not think that the court has jurisdiction of the issue: he believes that the question of

the division of a joint rate is for the Interstate Commerce Commission.* However, the Commission's power is confined to the division of "joint rates," appearing in "joint tariffs," and "joint tariffs" must contain the names of the participating carriers who must file their "concurrence or acceptance." The "Peoria's" name did not appear on the divisions of joint rates, nor did it figure in fact as a carrier at all; the "Central" divided the rate as though it was the carrier over the "Peoria's" rails. No doubt, the same considerations which enter into the Commission's divisions come up between the "Peoria" and the "Central"; but we are disposed to read the statute literally, as the Commission itself has done,** and to hold with the Master that it has no jurisdiction over the division of the "Central's" share between itself and the "Peoria."

(a) "Superimposition."

"Superimposition" is a name coined by the Bondholders to describe how the "Central" divided the proportion of joint rates which it received in cases where it was an "overhead" carrier: that is, when the shipment passed over, but did not begin or end on its own rails, but on the rails of the "Peoria." When the shipment left, or came upon, the "Peoria's" rails for, or from, those of an outside carrier the question does not arise, for the "Peoria" was allowed the "Central's" share; but that was not the case when the "Central" hauled a shipment over its own

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* §15(6), Title 49, U. S. Code.

** *Canton R. R. Co.* v. *Ann Arbor R. R. Co.*, 163 I. C. C. 263, 265-266, 267; *New York Dock Ry.* v. *Baltimore & Ohio R. R. Co.*, 73 I. C. C. 656.

rails as though it were an "overhead" carrier. As between itself and connecting carriers the "Central" succeeded in getting established as two blocks in the division of through rates, one block, Peoria to Danville—127 miles—and the other, Danville to Indianapolis—85 miles—which together made up the "Peoria's" total mileage—212 miles. Thus, if a shipment began or ended between Peoria and Danville, the "Central's" share of the joint rate had a credit of 127 miles, and if between Danville and Indianapolis, of 85 miles, which the "Central" collected for itself. In accounting to the "Peoria" for the income so received the "Central" did not, however, credit it with the amounts so collected; but in place thereof it substituted what it somewhat naively called "Family Percentages." It divided the whole road into three blocks, of which the middle and eastern were each seventy-five miles, and the western, sixty-two; and it computed the credits to the "Peoria" for terminal shipments as though these had been the blocks on which its own share of the joint rates had been computed. The Bondholders have christened these substitutions as "superimpositions," and say that they were "unfair."

So far as we can see, the "Central" does not really seek to defend this substitution beyond suggesting that in the end things probably evened up, the "Peoria" gaining upon some shipments what it lost upon others. That however is not an answer unless the practice was defensible in itself; and if it was not, the account must be to this extent restated. The Bondholders do not question the propriety of the divisions of joint rates between the "Central" and connecting carriers, including the blocks made use of for that purpose; but they say that the "Peoria"

was entitled to the same amounts which the "Central" secured by those divisions. Whether the "Family Percentages" were "fair," depends—under the standard we have set—upon whether, had the "Peoria" been negotiating divisions of the joint rates as an independent carrier, it and the "Central" would have agreed upon the same two blocks that the "Central" and the connecting carriers had agreed upon. The Bondholders did not indeed prove that this would have been the result of free higgling between the two; but we think that, as the record stands, the evidence was strong enough to put the "Central" to a rebuttal which it did not make. It cannot deny that the blocks, as between itself and the connecting carriers, provided "fair" compensation for the added costs of handling shipments at either end of the haul; yet those costs presumably would have been no less, had the "Peoria" been an independent carrier. That being so, it is a reasonable inference that either by bargaining, or by recourse to the Commission, the "Peoria" could have secured recognition of the same blocks, had it been dealing with the "Central." Notwithstanding that upon this, as the other issues, the Bondholders have the burden of proof, we hold that the evidence supported a positive inference upon the issue.

Nor are we embarrassed that the Master found against the Bondholders. Into his general finding that the use of the "Family Percentages" was justified, there necessarily entered a legal standard, or "norm," and such findings do not have the protection of the rule.* We hold that

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* Rule 53(e)(2); *Barbarino* v. *Stanhope S.S. Co.*, 151 Fed. (2) 553, 555 (C. C. A. 2); *Kreste* v. *United States*, 158 Fed. (2) 575, 577 (C. C. A. 2); *Guerrini* v. *United States*, 166 Fed. (2) (C. C. A. 2).

during the years that are open—1933 to 1945 inclusive—the income of the "Peoria" must be recast so as to credit it with "inflated mileage" based upon two blocks divided at Danville; but the Bondholders will share in this only from January 1, 1942.

(b) "Minimums."

The Bondholders' claim as to "minimums" is that the "Central" could have obtained for the "Peoria" "minimums" based upon the blocks which it used, taken without including any other mileage. Ordinarily, as we have said, when a shipment passes over a whole block, and begins or ends within another block, both of the same carrier, the "minimum" is based upon the combined mileage of both blocks; it is this combined mileage which must fetch twenty per cent of the joint rate, whether or not the mileage of that block alone on which the shipment begins or ends fetches twenty per cent. In its divisions with connecting carriers the "Central" made no effort to secure "minimums," based upon the mileage over which shipments passed on the "Peoria's" rails, and this failure is the basis of the claim. We do not understand that the Bondholders go so far as to say that, for example, the "minimum" upon a shipment coming from east of Indianapolis and ending west of Danville ought to have been based on the block between Danville and Peoria; but it does assert that it should have been based upon the whole mileage of the "Peoria" as it would have been had the "Peoria" been independent.

There was indeed evidence that in several cases the "Central" had secured "minimums," based upon the com-

bined mileage of a division, treated as though it were an independent carrier. Particularly striking was the case of shipments beginning or ending on the Springfield Division and passing through Cleveland; and there were other instances also. The "Central" replies that in all these cases the practice had been carried over from a time when the mileage on which the "minimum" was computed, had been that of an independent carrier which had been later consolidated with the carrier which was party to the division. That was the case with the Springfield Division, although the date at which the practice began of basing "minimums" upon that division alone is uncertain. The evidence is baffling and unreliable, and certainly before the Cleveland, Cincinnati, Chicago and St. Louis Railway Company was united with the New York Central Railroad in 1930, we should be unwarranted in saying that the first of these two roads could have secured "minimums" from the second, based upon the mileage of both blocks of the "Peoria." Moreover, the Master found otherwise. The Bondholders, however, argue that at least after 1930, when the two systems united, it must have been possible for the New York Central itself to grant such "minimums" upon hauls which began or ended on its own rails. That is of course true, but it does not follow that it became the "Central's" duty to do so. The situation thereafter can be looked at in two ways: either as though the "Central" were a single system after a merger; or as though the Cleveland, Cincinnati, Chicago and St. Louis Railway Company retained the independent existence it had had before. On the first hypothesis the "Peoria" had become functionally a division of the new system, enlarged by the addition of the New York Central Railroad, and there

was no more reason to establish "minimums" upon shipments beginning or ending on its rails than there had been before 1930 on the shipments beginning or ending on the rails of the Cleveland, Cincinnati, Chicago and St. Louis Railway, which the Bondholders do not claim. On the second hypothesis, although the New York Central Railroad would be regarded as a connecting carrier (as it continued to be regarded for other rate divisions) that is a fiction which should be consistently applied; and, if so, there is no more reason for saying that it would have conceded "minimums" upon shipments beginning or ending on its rails, than before 1930. On no theory did the Bondholders prove that the "Central" was negligent in failing to get "minimums." Finally, there is a clear distinction between "minimums" and "superimpositions," for the claim to the second is for revenues which the "Central" actually received.

(c) "Equalization."

"Equalization" is another word, coined by the Bondholders to describe the following situation and their proposed remedy for it. It applies for the most part, if not altogether, to shipments originating on the "Peoria," and bound over the "Central's" rails to a connecting carrier. It often happened that, if these shipments had left the "Peoria's" rails for an immediate connecting carrier's, the "Peoria's" share of the joint rate would have been larger than when they went first over the "Central's" rails, and thence to those of connecting carriers. The "Central" routed all shipments (so far as it could, for the last word is always the shipper's) over as much of its own rails as it

could, since that brings in the largest income to the system as a whole. The Bondholders do not complain of this; they agree that the "Central" was free to route shipments so as to get the most return; but they do complain that it was not free to do this at the "Peoria's" expense. By "Equalization" they mean a surcharge in the accounts which shall return to the "Peoria" those parts of the joint rates which it would have got, had the shipments been routed as the "Peoria's" traffic manager, acting as the agent of an independent carrier, would have routed them.

The claim would in any event be practically extremely difficult, if not impossible, to liquidate, because no one can now say how many of the shipments in question the shipper would not independently have routed just as they were in fact routed. However, the claim is invalid anyway; for once it be conceded that the "Agreement" authorized the "Central" to route the shipments with an eye to the interest of the system as a whole, the rest follows. If we assume that the "Family Percentages" have been corrected, the "Peoria" will have got its proper share of the joint rate over the route actually used. If it was not a breach of the "Agreement" to choose that route, there was no breach of any kind; and, if the "Peoria" is to recover more it can only be through an implied promise, to add an imputed income calculated upon income never earned at all. There is no possible basis for such a promise; on the contrary, whatever the financial incidents of a choice of routes consequent upon unitary operation, the "Agreement" included them; for it did not deny to the "Central" any part of the profit whose prospect had determined its choice of routes. The tail went with the hide.

(d) Grain.

These claims are in the same class as other "equalization" claims with one exception—"Grain Transited at Indianapolis and Reshipped to Chicago." Disregarding this for the moment, the practices complained of were reasonable, viewed from the interest of the "Central" although they did not result in that profit to the "Peoria" which, we will assume for argument, it could have made, had it been acting independently. Yet, once more, all that the "Peoria" may demand was that the "Central" should treat it in the same way that it would, had it been a wholly owned division.

The claim for "Grain Transited at Indianapolis and Reshipped to Chicago" stands on a different footing. The "Peoria's" share of the rate was fixed subject to an agreement between the "Central" and the Illinois Central Railroad, going back of 1890; and, in spite of the "Central" privilege to treat the "Peoria" as a wholly owned division, the single "management" authorized did not include allowances against the "Peoria" for payments to which the "Central" for its own purposes had previously committed itself. On the contrary, "management" is to be understood as usual or standard management. Indeed, neither the "Central" nor the Master, seem to defend these charges.

(e) Coal.

The Bondholders complain that the "Peoria" was not properly credited for the coal coming from mines lying to the southeast, which was paid for on the basis of the "Family Percentages." The accounts would of course have to

be restated like those for other merchandise, if it appeared that the joint rates on coal had been divided in the same way as the rates on merchandise. That does not appear; because of the loss of the "authority files" it is impossible to know on what basis the joint rates on coal were in fact divided, and the record is bare of any evidence showing that the "Peoria" was deprived of what it could have obtained as a connecting carrier. Here as elsewhere the burden of proof was upon it, nor can we use the disappearance of the "authority files" to throw any presumption upon the "Central."

The Bondholders seek to supply this absence of evidence as follows. The "Central" received for coal delivered by it at Indianapolis the same sum in dollars that it took upon coal passed to the "Peoria" rails at Indianapolis. If it was content with that division for coal delivered at Indianapolis, it must have been overpaid upon that which it passed to the "Peoria," for the cost of terminating a shipment is substantial. Hence it follows that on coal passed to the "Peoria" it got too much. This might be difficult to answer, if we knew that the "Central's" terminal costs upon Indianapolis deliveries were not made up in some other way; but we do not. So far as the record shows, Indianapolis may have been the far end of a block, in which event terminal costs would not have been allowed, being "absorbed" by the "inflated mileage" allowed upon shipments delivered at eastern points upon that block.

The Master found the evidence too uncertain for any conclusion that the "Peoria" had not been "fairly" treated; and we should not be warranted in saying that this was "clearly erroneous."

V.

Traffic Expenses.

The Bondholders challenge the "Central's" charge against the "Peoria" for traffic expenses upon the ground that it had been a faithless fiduciary, and as such is not entitled even to its expenses. It is true that a fiduciary may not be paid for services in whose discharge he has been disloyal; and at times, if his conduct has been wilful and deliberate, he may even forfeit all compensation:* but it is at least doubtful whether in any circumstances he will lose his right to indemnity for any expenses which have actually benefited the beneficiary,** though of course the beneficiary may set off against these any loss that he has suffered.† That the traffic expenses were to some extent beneficial to the "Peoria" goes without saying; on the other hand the "Central's" conduct might have shown such a wanton disregard for the "Peoria's" interest that the burden would rest upon it to single out that part of the expenses which were a benefit; and since it has not done so, it might be allowed no expenses. At least that is the most plausible argument for this extreme result. Be that as it may, we agree with the Master that the claim based upon supposed misconduct "is entirely without substance." True, the "Central" did not credit the "Peoria" with all the income that at the end of this exhaustive inquiry we have concluded was its due; but the Master, in a report of unrivalled care and acumen, exonerated it in all but a few details and those ancient ones. We can find no justification

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* *Restatement of Agency*, §469.

** *Restatement of Agency*, §439(c).

† *Restatement of Trusts*, §244.

for saying that it ever deliberately tried to despoil the "Peoria"; or that the matters with which we do charge it show evidence of any corrupt purpose. The "Agreement" put it, and was deliberately meant to put it, in an equivocal position; it was to serve two masters; and on the whole it acquitted itself creditably in a long series of extremely complicated transactions. To deny it its proper expenses would be to the last degree unjust.

There is however one specific correction which must be made. Until January 1, 1935, the "Peoria" was charged with the whole expense of the agencies maintained not only at Indianapolis and Peoria, but at Pittsburgh and Minneapolis. This was clearly "unfair," and indeed, so far as concerned the last two, it was the most indefensible act in the whole of the "Central's" conduct. The Master held that, except for the Statute of Limitations, the account would have had to be restated and these charges prorated as the other expenses were prorated. We agree; but, since even for the minority shareholders we go back only to January 1, 1933, the restatement will be confined to 1933 and 1934.

VI.

Harrisburg Coal.

This claim rests upon the argument that it was "unfair" to the "Peoria" to impose upon it the carriage of coal from the Harrisburg region which the "Central" found it to its interest to haul at a loss. As appears in the footnote, if the Master's findings are right, the traffic was not carried at an actual "out of pocket" loss; at worst it became a loss only after fixed charges and perhaps upkeep

were deducted.* The Bondholders say that, although it may have been proper enough for the "Central" to accept the shipments for the sake of the indirect advantages that would come to it, it was not entitled to put off such burdens on the "Peoria." This is the same argument that they used as to "Equalization"; and it equally disregards the purpose of the "Agreement." The "Peoria" had embarked in the same ship with the "Central" on a voyage which was in fact not to end for seventy years, and during that period their fate was to be one. What was good for the system was by hypothesis good for both; the advantages could not be separated.

Indeed, it does not certainly appear that, had the "Peoria" been independent, it would not have accepted the same traffic at the same loss. It had been an unsuccessful road, ending in bankruptcy; what would have been its bargaining power against the "Central," and whether it might not have found it desirable to accept some traffic at a loss in the hope of advantages to come, who can say?

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* Gross revenue per ton mile—3.26 mills. Deducting Peoria switching charges, charges due other roads and per diems, the net revenue is 2.18 mills per ton mile.

Average cost per ton mile (all freight)	2.50
Less Danville switching**	.425
Net cost per ton mile	2.075
Less 4% saving for heavy freight	.083
Corrected cost per ton mile	1.992 mills.

Net revenue	2.18
Net cost	1.992
Net gain	.188 mills.

** This item was not shown to have been absorbed by the "Peoria."

VII.

Freight Car Hire.

The background of this claim, which the Master has well sketched, is the complicated pattern of railroad practice as to the interchange of freight cars and charges for the use and handling of foreign cars. For each foreign car on its rails each railroad pays a rental charge which, being computed on a daily basis, is called a "per diem." This is designed to pay the owning railroad for the cost of ownership without allowance for profit; and during the period here involved the charge was $1.00 per day. Copies of interchange and junction reports are furnished each owning and using railroad, showing when each car passes from the rails of one to another; the balances, on monthly reports showing how many days each foreign car has been on the rails of each railroad, are settled by payments. The liability for "per diems" extends even to all home-bound empty cars, thus furnishing incentive for their prompt return to their owners. Home-bound "empties" are of two classes; (1) those which return by the same route they followed in their out-bound movement under load, and which are said to have "record rights" over each railroad participating in the movement under load, and (2) those which return over a railroad which had no part in the movement, and hence in the revenue, of the movement under load, which are said to be "out-of-route," or without "record rights." Each railroad is required without direct compensation for the service to receive at any junction on its lines all returning "empties" which have "record rights," and to move them along their home-

ward journey, paying "per diems" on them. However, a railroad is not obliged to accept "out-of-route" "empties"; nevertheless, if it does, it makes itself liable for "per diems," though it is paid by a haulage fee usually of six cents a mile.

Within the "Central's" system, each component division was treated as a separate entity as to interchange reports and "per diems." Thus the "Peoria" paid "per diems" to the "Central" for system (other than "Peoria") cars on its rails and the "Central" paid the "Peoria" for "Peoria's" cars on system (other than "Peoria") rails. As the Master recognized, the general arrangement obtaining under the "Agreement" was such that the "Central" had both opportunity and incentive to shunt to the "Peoria" a part of the cost of its own freight car hire. For example, in slack seasons when the "Central's" supply of freight cars exceeded its needs it was possible by an abuse of its managerial power over the "Peoria" to store its cars on "Peoria" rails longer than necessary, and to make the "Peoria" an involuntary bailee paying "per diems" on cars, for which neither "Peoria" or the "Central" had any immediate need. On the other hand, efficient management would often make it uneconomical to move system cars off the "Peoria's" rails, until it was known where they would be needed; for such movements obviously might result in waste motion. To reconcile economical operation of the system as a whole with the rights of the "Peoria" securityholders the "Central" devised a storage arrangement by which in slack seasons the "Peoria" was allowed credits known as "reclaims," also computed at the rate of $1.00 per day, per car, which re-

troactively cancelled out all "per diems" on system "empties" which had been on the "Peoria" rails over three days. It is this arrangement, though born of solicitude for the "Peoria's" rights and within the system applied only to the "Peoria," which is at the bottom of the Bondholders' claim of excessive car hire.

First it is objected that the storage arrangement was "unfair" in that the "Peoria" station masters for whose shortcomings the "Central" was legally responsible, often neglected to make the so-called "Form B" reports, with the result that "reclaims" even when allowable were not recorded and credited. In support of this charge, the Bondholders rely in part on a report made by a "Central" official named Bowen, who, when assigned to the service of the "Peoria" in 1935, made a report showing that in the first ten months of that year allowable "reclaims" aggregating $23,000 had not been credited. However, promptly upon the submission of Bowen's report these credits were allowed, and that episode, without more, is not adequate basis for an inference that at other times the agents were guilty of laxity which escaped the scrutiny and correction of supervising officials such as Bowen.

The Bondholders' claim is also based upon a study made for purposes of this controversy by their expert, Eppler. This study, it is true, showed that in January, 1940, some 492 system "empties" were handled by the "Peoria" for which it was charged "per diems" without offsetting "reclaims" credited in that month. There was, however, evidence that these charges were offset by credits allowed, which did not appear in the books until the following March. The Master took this evidence as sufficient to vindicate the

"Central" as to that item. This evidence was plausible and we cannot say that his conclusion was "clearly erroneous." The evidence disclosed a similar situation for January, 1942, which he similarly disposed of; and there was no other evidence of any specific instance in which allowable "reclaims" had been lost to the "Peoria" either because of laxity of personnel in making the required storage reports, or because of refusal to grant the credits when reported.

The Bondholders next attack the basis for the allowance of "reclaims" because they were allowed only when the "Central's" manager of freight transportation determined that there was a surplus of cars. Obviously, that was not inherently unfair; for during seasons of car shortage, when the management was pressed to find enough cars to handle its business, it was hardly likely that it would cut off its nose to spite its face by storing its cars on the "Peoria" even though it received "per diems." Only in times of car surplus did the "Peoria" have practical need for protection from possible abuse of the "Central's" power; and there was no evidence of any such abuse by freight managers who falsely or capriciously denied that what was in fact a season of surplus, was one.

Equally untenable is the Bondholders' criticism of that feature of the storage arrangement whereby the "reclaims" were limited to "empties" which had been on the "Peoria" rails for over three days. Their position is that no charge at all should result to the "Peoria" on system "empties," —even those which were on its rails for three days or less. The reasonableness of this contention is neither self-demonstrative nor actually demonstrated. Even with re-

spect to times when there were surplus cars, there is no evidence, either that the "Central" went to the trouble or expense of hauling un-needed "empties" on to the "Peoria" rails or that system cars, before or after loading or unloading on "Peoria" rails, were detained for two or three days without regard for the "Peoria's" needs, in order to furnish a basis for "per diems," or otherwise for the "Central's" convenience. So far as appears, even in times of car surplus the availability of some such cars may have been of benefit to the "Peoria": if there were times, when notwithstanding its own meagre ownership of cars, the "Peoria" had no need for system cars, there was no evidence that three days was on the average an excessive time for their removal under reasonably efficient management.

Somewhat more plausible is the complaint as to homebound "out-of-route" system "empties" handled by the "Peoria." The point is illustrated by the Eppler study for January, 1940, mentioned above, which showed 492 "empties" on the "Peoria" rails in that month, none of which, before or after their detainer, were used in the service of the "Peoria." At first glance it would seem unfair that the "Peoria" should be saddled with the cost of handling such cars or that it should be liable for their storage on the "Peoria" rails even for three days. Beyond dispute, such a burden on the "Peoria" was of substantial dimensions and was one that if independent it could have escaped. But, as the Master observed, under joint operation the "Peoria" enjoyed certain compensations which worked to offset that burden. For instance, the "Central" paid the "Peoria" "per diems" on the "Peoria" "empties" which it hauled

"out-of-route," and made no haulage charge for such service. And much more important, under joint operation the "Peoria" was not called upon to handle at all many system cars having "record rights" over the "Peoria," which if the "Peoria" had been independent would normally have been returned only at a "Peoria" junction. This is so because under joint operation the "Central" surrendered the right, which it had theretofore enjoyed, to refuse to accept for free haulage cars having "record rights" over the "Peoria"; consequently such cars could be returned at any system junction as well as to the "Peoria." Thus, during January, 1940, when the "Peoria" handled the 492 system "empties" without pay, an even greater number of system cars having "record rights" over the "Peoria" were returned via other routes, exonerating the "Peoria" from all charges and costs, for which, if independent, it would probably have been liable.

To be sure, the evidence does not go so far as to show the amount of these compensatory factors or of any others; but on the other hand there is a similar dearth of evidence as to the expense falling upon the "Peoria" under joint operation which it would have escaped if independent. The quantities on both sides of the ledger are undetermined and on the existing record are undeterminable. With the proofs in such a state it cannot be said that the Bondholders have sustained the burden of proving a breach of duty by the "Central" in this regard.

Careful consideration of the evidence and argument of the Bondholders cannot serve to alter this conclusion. It is true that there was written evidence that in 1935 Jackson, then the "Central's" superintendent of car service, and as

such an accounting rather than an operating officer, had some feeling that the "Peoria" was entitled to be relieved of all "per diems" on "out-of-route" system "empties," irrespective of the duration of their storage on the "Peoria" rails. Apparently he perceived that under the "Central's" Home Route Circular which was issued in May, 1935, the "Peoria" would be required to receive "out-of-route" system "empties," but for aught that appears, he wholly failed either to perceive or consider the compensatory features of joint operation. In any event, opinions expressed in 1935 and arrangements temporarily resulting from them, which were not repeated or justified in 1946 when the witness was under examination in an adversary proceeding, were certainly not binding on the Master or the court, and are not of controlling weight.

Nor is our conclusion at variance with the effect of the Bowen report of 1935 pursuant to which the "Peoria's" storage credit for a ten months' period was increased by $23,000. We agree with the Master that it is impossible to find from the evidence upon what basis that adjustment was made: certainly it was in large part a correction to credit "reclaims" previously unreported through inadvertence. We cannot view it, however, as an admission that throughout the relevant period it was unfair to charge the "Peoria" with "per diems" on cars detained on the "Peoria" rails for not over three days; still less as an admission of controlling weight on the ultimate issue.

The Bondholders' claims directed particularly to the allegedly excessive charges for car hire in 1924 and 1925 are foreclosed by the accounts stated; and such claims would not be available to the minority shareholders because

of the Statute of Limitations. That is so, quite apart from the fact that counsel for the "Peoria" makes no claim of any kind for excessive charges for car hire.

On their brief, the Bondholders seem not to pursue their claim of unwarranted storage charges against the "Peoria" on account of system cars while being repaired in its Urbana shop, or of system "empties" stored at Indianapolis or Danville. In any event, the claims as to those items, if not abandoned, are overruled. We find nothing in the record which would justify us in disturbing the Master's conclusions on these points. Indeed, our ruling as to the burden of proof is decisive here.

VIII.

Equipment Repair Costs.

From 1921 to 1942 the "Central" charged the "Peoria" $3,610,897.01 for freight car repairs. The Bondholders point to the fact that this figure exceeded by $1,123,452 the average for all Class 1 Railroads on a per car basis, and without further reference to specific figures they claim that the "Central" has failed to justify its charges. The claim is apparently predicated upon that covenant of the "Agreement" under which the "Central" was to "keep up and maintain all said * * * line of railroad and all said rolling stock and equipment in good working order, and restore and renew all parts thereof as may be necessary to that end." This covenant of course imposed a duty upon the "Central" to do the repair work now in question with reasonable efficiency, but the burden of proving a breach was on the Bondholders; and they have failed to carry it.

Indeed, they expressly conceded that, "because of the unavailability of detailed records," they "were unable even to approximate the extent" of a proper surcharge. Except for the year 1942, our holding as to the finality of the accounts would alone be a defence; and, incidentally, if the dearth of evidence is due to the loss of the "Central's" records, it confirms the wisdom of the mortgage draftsman and the inherent justice of foreclosing those who for so long assented to the correctness of the transactions recorded.

IX.

Demolition of Moorefield Terminal.

The Bondholders assert that the accounts should be recast to charge the "Central" with $240,000, the difference between the estimated cost of replacing an engine terminal at Moorefield and the cost of repairing it in the year it was abandoned. This was originally built in 1889 at a cost of $41,831; and by 1934 had become obsolete. The engine stalls were too small for the locomotives then in use, and a public street prevented their enlargement which would in any event have involved expensive changes in the water station and coal dock. For these reasons in 1934 the upkeep and repair of the "Peoria" locomotives was transferred to "Central" shops, resulting in improved service at less expense; and in 1941 the old terminal was demolished, and no substitute has as yet been either needed or provided.

The "Agreement" does not expressly require the "Central" to keep up all existing buildings; nor do we

think that the promise "to restore and renew" bound the "Central" to build a new terminal on the "Peoria" line, if it was not practically feasible to enlarge the old one. Article Third of the "Agreement" treats the cost of "reasonable betterments" as an expense to be borne, it is true, by the "Central" in the first instance, but recoverable out of net earnings if, and as, any such should accrue.

However, it is not necessary now to decide these questions. For until the responsibility for operation reverts to the "Peoria" it can suffer no damage from demolition of this obsolete engine house; not until then will it be known what will be its needs upon resumption of operations. Not until then will it be faced with a predicament analogous to that of the Old Colony in the New Haven reorganization proceedings.* Even without applying the rule of accounts stated, no case was made as to this item.

X, XI and XII.

Intercompany Sales of Rolling Stock.

Both the Bondholders and the "Peoria" challenge the Master's conclusions that the "Peoria" has been charged with no more than fair prices in its purchases from the "Central" of certain rolling stock. All of this equipment was sold before 1942; and it follows that the accounts bar any claim by the Bondholders. However, if the claims are allowable on the merits, in so far as they are not barred by the Statute of Limitations our earlier ruling would allow

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* *Old Colony R. Co.* v. *N. Y., N. H. & H. R. Co.*, 98 Fed. (2) 670 (C. C. A. 2) (reversed on grounds not relevant here, 305 U. S. 578).

them in favor of minority stockholders. We proceed, therefore, to a consideration of their substance.

The "Peoria" suggests that these transactions, which were sales by subsidiaries of the "Central" to the "Peoria" —because they were not required or contemplated by the "Agreement"—are to be tested by a stricter standard than that governing transactions covered by the "Agreement": i.e. by the rule of *Geddes* v. *Anaconda Copper Mining Co., supra,** and *Chelrob, Inc.* v. *Barrett.*** On the contrary we think it fairly inferrable that the reorganization of 1890 regarded it as one of the economies of joint operation that, when the "Peoria" needed additional rolling stock, second-hand equipment might be sold to the "Peoria," when it had become less serviceable for use where it was than it would be when sold. That appears to us to be a legitimate incident of the joint management which was the prime purpose of the whole enterprise. We hold, therefore, that as to these sales there is no occasion to deviate from the standard which we laid down earlier, or to shift the burden of proof.

Coming then to the substance of these claims, we find sufficient support for the Master's findings of fact. Of the locomotives, thirty-four were sold at prices based on depreciated ledger values, six at prices based on depreciated ledger values less an allowance for run-out repairs, five at prices based on the approximate depreciated ledger values and eleven at prices based on scrap value. In this connection it is not necessary for us to decide whether reproduction cost less depreciation should have been used

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* 254 U. S. 590.

** 293 N. Y. 442.

as the principal factor of valuation instead of depreciated ledger value, because, as the Master found, the use of reproduction cost less depreciation at rates authorized by the Interstate Commerce Commission even with deduction for the cost of run-out repairs, would have resulted in a higher sales price than that actually adopted. It is true that the bondholders presented plausible expert testimony tending to show that the actual sales price had been somewhat excessive. But this testimony was based upon a highly complicated formula which had been developed by an expert when engaged as a locomotive sales engineer, and which had never been tested in actual practice by any railroad. The Master's preference for a more familiar basis of valuation has solid support in the record. We affirm his conclusion that an excessive price has not been proved.

In fixing the price of the sale of the 417 box cars and fifty hopper cars the "Central" was not precluded from using as a basis, cost less depreciation at 3%, with a thirty-year life and a 10% salvage value, merely because the depreciation had been accrued on its books at a somewhat higher rate. The earlier treatment of similar inter-company transactions which fixed the price on another basis does not show that the Master's findings were "clearly erroneous." Moreover, the selection of a higher depreciation rate was apparently based upon inadequate experience, and is entitled to little weight, after later experience had justified that lower rate on which the actual sale price was computed. After thoughtful evaluation of a mass of conflicting evidence the Master was particularly impressed with the weight and the validity for present purposes of a rate of 2.6% recently adopted by the Arbitration Committee

of the Association of American Railroads. We confirm that view.

As to the fifty hopper cars the alternative claim, advanced by the counsel for the "Peoria," is barred by the ten-year Statute of Limitations: for the transaction in question took place in 1924. Of the nine passenger cars involved seven were sold before 1932, and the claim is barred under the Statute of Limitations. The remaining two, sold in 1938 on a basis of depreciated ledger value, do appear to have been sold at prices computed at an inadequate rate of depreciation; and the Master's finding of a thirty-year life for these cars was sufficiently supported. It follows, therefore, that these two sales should be recomputed and the accounts recast accordingly: attributing to these cars a thirty-year life (with the 10% salvage value which we take to be implicit in the Master's finding). We note that as to this item there was no evidence of value based upon reproduction cost; but that does not require that the record of fact be reopened: the parties have all had their day in court.

Lastly, except for credits aggregating $7,459.98 which the "Central" concedes, and except for a claimed overcharge of $144.04 in a Post Office car which, like the Master, we view as "de minimis," the "Peoria" objects to sales of seven gondola cars in 1940 and 1941; and for each it claims a credit of about $300. These were sold for conversion into flat cars, and, although the cost of conversion was far higher than originally estimated, the Master apparently found no evidence that the basic sale price was excessive. The mere fact that the eventual cost of conversion was greater than anticipated is not enough to constitute a breach of the "Agreement." We confirm the Master's report on this item also.

XIII.

Indianapolis Trackage Agreements.

For the complicated facts upon which this claim depends we refer to the Master's report. The Bondholders say that the trackage agreement of 1932 was a definitive contract, relating to the exchange of trackage rights east of the I. J. Tower, and that the consideration for what the "Peoria" got was to be what it then gave and nothing more. Hence, when the "Central" made the contract of 1940—"as of" 1936—it disregarded this original agreement, treating it as tentative, or only a negotiation. Thus they conclude that the "Central" exacted from the "Peoria" the trackage rights from the Brant Tower to the I. J. Tower, for which it gave nothing at all, and that this was barefaced spoliation. We will not decide this issue as things stand, for we agree with the Master that it involves something over which the Interstate Commerce Commission has exclusive jurisdiction. The Commission's order on April 8, 1940, granting a certificate of convenience and necessity for the exchange of trackage rights, expressly incorporated "the terms and conditions set forth" in its report; and the report described just what was to be exchanged and on what terms the tracks were to be used. In Transit Commission v. United States,* the Supreme Court held that a trackage agreement between carriers was as much within the jurisdiction of the Commission as the construction of new tracks. Congress intended to "confer upon the Commission plenary power to limit interstate carriers' expenditure for construction or operation to lines of rail-

* 289 U. S. 121.

road reasonably necessary for the service of the public," and there was "no room for a distinction between unjustifiable expenditures for the construction or operation of new mileage, on the one hand, and inadequate rentals or extortionate exactions under trackage agreements on the other" (p. 128). In a case closely akin—though it arose under another statute passed after the trackage agreement of 1940 had been made—Douglas, J., in speaking of the language we have just quoted, said:** "Those questions intimately relate to the financial strength of carriers. And it is one of the Commission's high functions to protect the public interest against unfair or oppressive financial practises. * * * That policy would be undermined if the carriers could repair to courts for determination of the conditions under which trackage rights could be secured."

In the light of these decisions it is of no moment now whether the Commission in fact considered the fairness of the agreement of 1940:—particularly whether the "Peoria" received any consideration for the added trackage rights which it gave in that year. Arguendo, we will assume that it may have known nothing about the earlier transaction; indeed, this seems not impossible, for the "Peoria" was apparently not independently represented. The important thing is that the Commission issued the certificate for that exchange of trackage which was before it for approval and for no other exchange; and that that exchange involved precisely those "terms and conditions" which it did involve and no other "terms and conditions." If we were to hold that the "Central" must make the added payment

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** *Thompson* v. *Texas-Mexican Railway*, 328 U. S. 134, 148.

which the Bondholders demand, we should vary those "terms and conditions," and that would be in effect to issue a different certificate. That we must not do—as little when the amount involved is small as when it is large—for all such questions are for the Commission. Recourse must be had to it, and it is premature to try now to declare what if any questions will be within our jurisdiction, should it issue another certificate. The case will be held open, if any party in interest wishes to seek the action of that tribunal.

XIV.

Claimed Adjustments Under the Indianapolis Trackage Contracts.

Notwithstanding our lack of jurisdiction to pass on the validity of the trackage agreements, we have, however, jurisdiction to decide any claims made under them, assuming that they remain unchanged. The Bondholders have made claims under the 1940 agreement, and the "Peoria" has made them under the 1932 agreement. Apparently through inadvertence the accounts had been cast without including any items under the 1940 agreement; and when this appeared at the hearings the Bondholders asked the "Central" to submit a statement showing what adjustments were necessary to give effect to that agreement. Before the hearings closed the "Central" did present such a statement covering the years 1936 to 1942; but it showed a balance of $19,312.22 in favor of the "Central." This the Bondholders attack, principally because it was based upon a wheelage study made in 1923 which had become stale. The Master, pointing to the lessened uses by the

"Peoria" of the trackage in question, agreed that the study was stale, and recommended that for future accounts a new study be made; but he refused to give any effect to it retroactively, when it is made. However, as we understand his ruling, he recommends that the "Central" be allowed the entire balance shown in the actual statement, submitted to him.

That statement was a charge against the "Peoria," composed of an item of rental for its use of the tracks, together with its proportion of the costs of upkeep, taxes and other outlays, all based on the stale study. Apparently, as we have said, the "Central's" omission to include the charges so resulting in its annual accounts with the "Peoria" was inadvertent; and it has been well-settled law from the beginning that the conclusiveness of an account stated yields pro tanto to mistakes.* However, although the "Central" was for this reason not bound by the omission, as a fiduciary of the "Peoria" it had the burden of proof, at least as to all items of charge;** and that burden it did try to carry by the use of the stale study of 1923. When that study was rejected as a basis, it had not proved the issue at all, so that the record, as it stands, does not support any claim against the "Peoria." This result is entirely consistent with our imposing the burden of proof upon the Bondholders and the "Peoria" in those cases where we have done so; for these were instances in which

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* *Perkins* v. *Hart*, 11 Wheat. 237, 256; *Oil Company* v. *Van Etten, supra*, 107 U. S. 332 (107 U. S. 325).

** *Woolton Land & Fuel Co.* v. *Ownbey*, 265 Fed. Rep. 91, 99 (C. C. A. 8); *Judson* v. *Buckley*, 130 Fed. (2) 174, 183 (C. C. A. 2); *Garrett* v. *First National Bank & Trust Co.*, 153 Fed. (2) 289, 292 (C. C. A. 5).

their claims were conditional upon some breach of the "Agreement," which is not true as to the trackage agreement. Thus, although we agree that the Master was right in refusing to extend the hearings so as to allow the preparation of a new statement, we think that he was wrong in allowing any credit to the "Central" under the one which it submitted.

The "Peoria," through its counsel appointed by the Court, has not joined in the requested adjustment under the 1940 trackage agreement. It has, however, claimed that the accounts should be corrected to surcharge the "Central" with a loss to the "Peoria" of $20,560 under the 1932 agreement:—this on the theory that that agreement must be treated as an independent, self-contained transaction. Whether or not this falls within the jurisdictional point we have disposed of under Point XIII, the claim is foreclosed by our ruling that the ten-year Statute of Limitations is applicable.

XV.

The Champaign Grain Elevator.

This item, pressed both by the Bondholders and the "Peoria," relates to a sale by the "Central" to the "Peoria" in 1916 and entered in the accounts of that year. It is foreclosed by our rulings upon the accounts stated and the Statute of Limitations.

XVI.

Peoria and Pekin Switching Charges.

This item depends upon the interpretation of a number of baffling documents, cast in the elliptical language of railroads, whose meaning is either completely unintelligible to laymen or can only be vaguely guessed. *Texas & Pacific* v. *American Tie Co.** first laid it down that documents, written in such terminology may be so obscure as to demand an acquaintance with the idiom of the calling and its practises and conventions, which are beyond the reach of courts. In that case the Court held that such an occasion arose when the question was whether railway ties fell within the classification of "Lumber" in a rate schedule. Another instance was *Standard Oil Co.* v. *United States,*** where a shipper argued that a shipment of petroleum products did not come within the tariff which the carrier had in fact used, because there were other and specific rates, "taking precedence which were lower and should have been applied." (p. 237). The Court held that the district court had no jurisdiction to review a ruling of the Commission that the products were subject to the tariff used, because the interpretation of the documents was for the Commission and was not a question of "law." In *Davis* v. *Age-Herald Publishing Company,*† the Fifth Circuit similarly held conclusive a ruling of the Commission that "printing paper" did not include "newsprint paper"; and in *Norge Corp.* v.

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* 234 U. S. 138.

** 283 U. S. 235.

† 293 Fed. Rep. 591.

Long Island R.R. Co.,* the Second Circuit decided that it was a question for the Commission which of several classes in a rate schedule applied to refrigerators. It is true that the words of a railway tariff do not inevitably demand recourse to the Commisison. *Great Northern Railway* v. *Merchants Elevator Company*** was such a case; it held that a court might decide for itself whether "disposition orders" included orders "by way of reconsignment to another destination," (p. 289), for the meaning of the words was apparent without the background of specialized experience. Nevertheless, Brandeis, J., recognized the doctrine in the following passage of his opinion: "Where the document to be construed is a tariff of an interstate carrier and before it can be construed it is necessary to determine upon evidence the peculiar meaning of the words or the existence of incidents alleged to be attached by usage to the transaction, the preliminary determination must be made by the "Commission." (p. 292).

In considering whether the interpretation of these documents is for the Commission we start with "Division Sheet No. 162" which, as we understand it, all agree to have spread the switching charges over all parties to the joint rate in proportion to the mileage of each. That was in 1916, and there had been a number of earlier division sheets of other roads which had recognized the practice. "Amendment 86" was issued by the Joint Rate Committee to take effect January 1, 1917, and, although its chief purpose appears to have been to fix the amount of the charges, at its bottom is a passage which at least suggests that these were

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* 77 Fed. (2) 312.

** 259 U. S. 285.

to be prorated. "Division Sheet I-A" was issued by the Railway Administration in 1919; it declared that the "allowances specified are to be made out of Federal controlled lines"; and this too seems at least to presuppose prorating the switching charges. The "Supplements" to "Division Sheet I-A" issued before "Supplement No. 7" are not important; and at any rate they did not weaken the force of the argument, which arguendo we shall accept, that up to 1922, when "Supplement No. 7" was issued by the two local roads, the tariffs contemplated prorating the charges. That "Supplement" did expressly "cancel" "Division Sheet I-A and Supplements," and the Master found that it also cancelled all authority for prorating the charges. The expert for the Bondholders believed that its effect was limited to cancelling the existing schedule of charges. He could find no documentary evidence in the "Central's" files to indicate that the practise of prorating had changed, and he thought that the former documentary warrant for it remained. The expert for the "Central" thought otherwise; and the Master apparently preferred him. Moreover, although it seems curious that the two local roads—owned in part by the "Peoria"—should have thrown the whole switching charge upon it, and that the "Central" should have given up passing on a part of that charge to connecting carriers, it is even stranger that for over twenty years all the roads concerned should have misapprehended the effect of the documents under which they were operating.

We can scarcely imagine a situation, calling more loudly for the intervention of expert opinion than this welter of papers, all expressed in the jargon of a vocation which has developed its own dialect, and all to be interpreted in

the light of practices which apparently went on for two decades after the last relevant document was issued. Whatever certainty is possible in such circumstances is obviously only in the possession of those who have become familiar with those "incidents" which have been "attached by usage to the transaction." The Master thought otherwise, because the Commission's jurisdiction was given to it only to prevent diversity of ruling and because the question would not arise again for it was "unique." It is indeed true that one of the most important reasons for vesting jurisdiction in the Commission was to secure uniformity; but that was not the only reason. It would be a sorry result to deprive the parties of the only really qualified tribunal because the injustice done by a mistake of an unqualified one will be limited to a single instance. We are not to confuse the extent of the Commission's jurisdiction with the motives which led to the Commission's creation. Besides, we do not see that our decision here would inevitably be "unique." If we took the Master's view that prorating had ceased to have any documentary warrant, although that might be final between the parties here, it might not satisfy the "Peoria"—now able to assert its rights—that it had no claims against carriers other than the "Central." And a fortiorari, if we held that prorating had continued to be the proper division, the "Peoria" might wish to assert the same claim. We will adopt the same course as to this item that we have as to the item depending upon the Indianapolis Trackage Agreement.

XVII.

General Expenses.

For over twenty years it had been the practice of the "Central" to ascertain and account for the general expenses of the "Peoria" on a mixed basis as follows: (1) general expenses directly incurred for the exclusive service of the "Peoria" were directly charged; (2) some general expenses not for the exclusive service of the "Peoria" were apportioned on some use or cost basis which happened to be available, and (3) joint general expenses incurred not for the exclusive service of the "Peoria," for which there was no available basis for apportionment, were divided on the basis of the ratio between the operating revenues of the "Peoria" and the operating revenues of the system.

The Bondholders contend that they should be exonerated from these charges for general expenses to the extent that they include a part of the salaries and expenses of officers of the system and their staffs, on the ground that certain of the officers have not "served the P & E properly in certain respects or during certain periods"; and that the "Central" should be treated as a faithless fiduciary. This is in effect the same objection which they made to the allowance of "Traffic Expenses," and what we have there said in answer applies with equal force here.

The Bondholders also contend that the general expenses charged against the "Peoria" were excessive; a charge which they base almost entirely upon a comparison of expenses with other railroads, having revenues comparable with the "Peoria." What it comes down to is that the

"Central" managed the operations of the "Peoria" with less than reasonable efficiency; and as to that the burden of proof was on the Bondholders. We agree with the Master that they did not prove their case. Indeed, as they themselves point out, the greater part of the putative "excess" expense is traceable to the Indianapolis office in which the work done was exclusively limited to the "Peoria"; and was necessitated by the accounting and auditing summarized in the annual statements. There was no evidence that this work could have been done at less cost if the "Peoria" had been independent; moreover much of it was an inevitable result of the "Agreement" which required revenues and expenses properly apportionable to the "Peoria" to be segregated from those of the system as a whole. That was a task which required extended computations, and hence, item for item, was more burdensome than the system accounting which did not require complicated and expensive allocations. Indeed, we question whether a finding of inefficient management may be based merely on a comparison with the operating results of other railroads: it may well be that such a comparison to have any appreciable weight requires a similarity in such a multitude of operating conditions that no other railroad offers a dependable standard. But if comparisons are to be made at all, the standards for comparison should be railroads whose accountings have involved some segregation of its share of the revenues and expenses of a larger system. That is an item which most solvent railroads escape; it is generally only in insolvency that the necessity arises in the accounts of mortgaged divisions and leased lines.

Taking into account the weight of all relevant evidence we hold that the Master's findings here too should be affirmed. Inefficient management not having been shown, it was not improper to charge against the "Peoria" the entire cost of services rendered exclusively for the "Peoria," and a share of the cost of system services determined by application of the ratio between system revenues and "Peoria" revenues.

XVIII.

Pullman Operations.

Both the Bondholders and the counsel for the "Peoria" asserted that charges in the accounts for Pullman car operations should be disallowed; such was the Master's conclusion, and the conclusion is not questioned by the "Central." Consequently, to the limited extent permitted by our rulings as to accounts stated and the Statute of Limitations the Master's conclusion is affirmed.

XIX.

Miscellaneous.

The Master's rulings as to interest, and the distribution of "government cutbacks" are also affirmed.

Unless the parties can agree upon the proper amounts to be entered in a decree, the cause will be referred back to the Master to state the accounts and to report a proposed decree in accordance with the foregoing opinion.*

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* The substance of Judge Hinck's original drafts discussing a number of items—notably VII—I have incorporated in the above opinion.

Ewen v. Peoria & Eastern Rwy.

I concur

ALFRED C. COXE
D. J.
April 16/48

Ewen v. Peoria & Eastern Rwy.

I concur

April 22, 1948

C. C. H.

OPINION—June 4, 1948 (R. 35)

Endorsed: U. S. District Court
Filed June 4, 1948, 11:15 A.M.
S. D. of N. Y.

[SAME TITLE]

Before:

L. HAND, COXE and HINCKS, JJ.

ON PETITION FOR REHEARING

PER CURIAM: The Bondholders have petitioned for a rehearing on our denial of minimums to the "Peoria," very largely repeating their former argument. They point out however that we were wrong in saying that there was no difference in the situation after 1930 if the "Central" be regarded as one system; we failed to notice that, so long as the "Big Four" and the "Peoria" formed a system separate from the New York Central system, it was not necessary for the "Big Four" to allow minimums to the "Peoria," for its share of the rate upon hauls ending upon "Big Four" rails was always at least twenty per cent of the whole rate. Therefore, the question does arise whether if, by the lease of 1930 the lessor and lessee became one road, it was an abuse of the "Central's" power over the "Peoria" not to allow it minimums over hauls in which the "Big Four" figured as an overhead carrier. As to this we are to apply the standard which we applied throughout: i.e. whether the "Peoria," assuming that it was an independent road could have exacted minimums from the com-

bined road—the "Central." Confining ourselves therefore to the period after 1930, and assuming that the lease of the "Big Four" to the New York Central Railroad gave the lessee a free choice to allow minimums, and that it might do so without recourse to the Interstate Commerce Commission, we are to say whether it should have done so; which means whether the "Peoria" has proved that in dealing at arms length with the "Central" it could have exacted this as a condition. The Master has found that minimums of twenty per cent were not by any means uniformly allowed to all small roads; and that the issue seems to have been a matter of private bargaining. The Bondholders point to the fact that the "Peoria" secured the minimum upon hauls that left its rails upon which the "Big Four" was not an overhead carrier, as evidence that it could have procured them at arms length bargaining. These minimums the "Big Four" secured for the "Peoria"; the "Peoria" did not secure them for itself; and the difference is extremely material. To take an instance which seems particularly impressive at first blush: the minimum granted by the Pennsylvania for traffic which left the "Peoria's" rails at Indianapolis. The argument is that the "Central" would have been obliged to meet Pennsylvania competition by a like concession; but it does not follow that the "Peoria" dealing with both the "Central" and the Pennsylvania would have been able to get a minimum—or at least a minimum of twenty per cent—from either of them. As we have said, there were a number of cases in which small roads could not do so. In the supposititious case we have made the test, we must imagine the "Peoria," not speaking as part of a great system, but

as a road 212 miles in length which alone had never succeeded in keeping alive. How can we measure the strength of its bargaining power?

Nor are those instances persuasive where divisions of a road continued to receive minimums after they had been taken over by another road. The Springfield division of the "Big Four" was such an instance; the minimum had existed since 1890 when the Springfield division was part of the same road as the "Peoria" itself. There were apparently a number of such cases; and, whether they were thought to be preserved under §76(b) of Title 49, U. S. Code; or out of mere conservatism; or for some other reason, does not appear; but at least they are not evidence which makes against the Master's finding that the Bondholders did not prove that a minimum of twenty per cent was the invariable or regular practise. But it may be said that the Interstate Commerce Commission might have intervened to compel the grant of such a minimum. There would indeed, upon the hypothesis we are assuming, have been a division of joint rates, and the Commission would have had jurisdiction; but we do not see that we have any indication as to how it would have exercised its power. So we conclude that, viewed as a question of what the "Peoria," if it stood alone against the "Central" could have secured, the Bondholders did not present a case which shows that the Master's finding was "clearly erroneous." That finding is one of fact in the strictest sense; it included no "standard," no "norm"; it was merely as to what was the practice of railroads.

Indeed, the question is more complicated than we have indicated. We have held that we could pass upon the divi-

sion of income received, because as between the "Peoria" and the "Big Four," as part of the "Central," there was no "division of 'joint rates,' appearing in 'joint tariffs'" which "contain the names of the participating carriers." However there continued to be "divisions of 'joint rates' appearing in 'joint tariffs'" between the "Big Four" and the New York Central Railroad, after the lease of 1930 as well as there had been before, and over these the Commission had exclusive jurisdiction. Any minimum granted by the New York Central Railroad, as lessee of the "Big Four," would affect the division of "joint rates" between itself and the "Big Four," and we should not have jurisdiction to pass upon it. At most we could say that the "Central" should divide the share of the joint rates which came to the "Big Four"—as between itself and the "Peoria"—as though the "Peoria" had been granted a minimum in a division between the three. That, however, presupposes that the Commission would have granted the minimum, had the matter come before it; and, as we have just said, that we cannot know. Moreover, although, perhaps in logic we should remain within the limits of our jurisdiction in making such a division, we should be really acting as a substitute for the Commission which we have not the competence to do. This difficulty cannot be avoided by saying that in fixing the division of the joint rate between the "Big Four" and the New York Central Railroad, the latter could, by consenting to give a minimum to the "Peoria," avoid the Commission under §76(b) of Title 49, U. S. Code. It is true that it was a lessee, but, since the two roads are treated for purposes of rate divisions as separate carriers, it is highly improbable that the New

York Central would be allowed to consent for the "Big Four" to a reduction in the "Big Four's" share, such as would result from the grant of a minimum to the "Peoria." Even as majority shareholder of the "Big Four," the New York Central Railroad could not lawfully give such a consent, unless the situation of the "Big Four" vis-à-vis the "Peoria" independently justified it. It would therefore seem to us that to the limited degree to which we can on any theory have jurisdiction, it is extremely doubtful that we should attempt to exercise it; even were we satisfied that the Master's finding was "clearly erroneous." Whether for the future the "Peoria" would have any standing before the Commission as a party interested in the division of rates between the "Big Four" and the New York Central Railroad, we cannot of course say; but on this record we see no reason to change our first decision.

Petition denied.

STIPULATION—October 15, 1948 (R. 37)

[SAME TITLE AS FINAL DECREE]

WHEREAS, the Court, in its opinion dated April 24, 1948, found that there should be a recasting of the intercompany accounts between the Peoria and Eastern Railway Company, on the one hand, and the New York Central Railroad Company and the Cleveland, Cincinnati, Chicago & St. Louis Railway Company (Big Four), on the other, for the years 1933 through 1945 to reflect a reallocation of freight revenues (1) accrued from the transportation of "Grain Transited at Indianapolis and Reshipped to Chicago" and (2) in accordance with the claim of "Superimposition", as those claims were defined and allowed in the opinion of the Court, and

WHEREAS, the parties to this stipulation have made test samplings of these accounts considered adequate by their accountants and attorneys, and

WHEREAS, the New York Central Railroad Company and the Cleveland, Cincinnati, Chicago and St. Louis Railway Company (Big Four) have concluded from their tests that such a recasting of accounts will produce no additional revenue or income for the Peoria and Eastern Railway Company, and

WHEREAS, the Peoria and Eastern Railway Company has concluded that such a recasting of accounts will produce no additional revenue or income for it, and

WHEREAS, the Income Bondholders of the Peoria and Eastern Railway Company have concluded from their tests that such a recasting of accounts, without the application of other principles of allocation of freight revenue which were contended for by the Income Bondholders but which were rejected by the Court in its opinion herein, would produce no change in the freight revenue account of the Peoria and Eastern Railway Company sufficient to warrant the expenditure necessary to determine the precise effect of the opinion of the Court,

IT IS HEREBY STIPULATED AND AGREED by and between the New York Central Railroad Company, the Cleveland, Cincinnati, Chicago & St. Louis Railway Company (Big Four), the Peoria and Eastern Railway Company and the Income Bondholders, by their respective counsel, that such a recasting of the items above mentioned, as allowed by the Court in its opinion herein, without the application of other principles of allocation of freight revenue which were contended for by the Income Bondholders but which were rejected by the Court in its opinion herein, would produce no change either way in the freight revenue account of the Peoria and Eastern Railway Company sufficient to warrant the expenditure necessary to determine the precise effect of the opinion of the Court,

AND IT IS FURTHER STIPULATED AND AGREED that with respect to the items above mentioned, as allowed by the Court in its opinion herein, no recasting or revision of the intercompany accounts for the years 1933 to 1945 inclusive shall be made,

AND IT IS FURTHER STIPULATED AND AGREED that this stipulation may be filed with the Court as part of the record of this proceeding.

Dated: New York, N. Y., October 15, 1948.

/s/ CHARLES S. ARONSTAM,
Attorney for the Income Bondholders of the Peoria & Eastern Railway Company.

/s/ GERALD E. DWYER,
Attorney for The New York Central Railroad Company and the Cleveland, Cincinnati, Chicago & St. Louis Railway Company.

/s/ F. W. H. ADAMS,
Attorney for the Peoria & Eastern Railway Company.

OPINION—November 16, 1948 (R. 38)

[SAME TITLE AS OPINION—APR. 24, 1948]

Before:

L. Hand, Coxe and Hincks, JJ.

Per Curiam: It is true, as the Bondholders say, that the New York Central Railroad Company had power at any time to withdraw any part of the "special account" set up on August 3, 1943, and the later additions made to it; but, if any such withdrawals would have been a violation of Section 24 of the decree of July 23, 1940, as amended on April 3, 1941, the account was available only by a contempt of court, and we cannot rate among its quick assets what the road could only touch under peril of penalties, pecuniary and personal. That any withdrawals would have been in violation of the decree can be easily demonstrated.

The last sentence of Section 24 of the final decree as it stood originally read as follows:

> "Should the New York Central Railroad Company and/or the Big Four seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said intercompany accounts, then and in such event said New York Central Railroad Company and/or Big Four must prove and establish their right to do so."

The amendment of April 3, 1941,—made at the demand of the Bondholders—inserted before the nine concluding words the phrase: "upon objection by the representative of the Income Bondholders elected to the Board of Directors".

Perhaps the change did no more than make express what was already implied; be that as it may, there can be no debate that after the amendment the Bondholders acquired power to forbid the New York Central Railroad Company to "withdraw any part of the earnings" of the Peoria and Eastern Railway Company until it had proved itself entitled to withdraw them. The Bondholders by their successive objections exercised that power, and the New York Central Railroad Company opened the "special account" in compliance.

The Bondholders answer that, granted as much, to open a "special account" was not to impound funds by putting them outside the power of the depositor; compliance was merely a matter of "bookkeeping". Of course, it was merely a matter of bookkeeping, as it would have been, had the deposit been made in the joint names of the New York Central Railroad Company and the Peoria and Eastern Railway Company; but the objection disregards the very substance of the issue. The whole business of the railroad must be conducted as a "matter of bookkeeping"; and to deprive itself of the power to make use of any part of its bank deposits was the precise equivalent of withdrawing the same number of dollars, putting them into a safety deposit box, and giving the key to the marshal. We hold that the Bondholders and the Peoria and Eastern Railway Company are not to be credited with interest on the "special account".

Dated: November 16, 1948.

PETITION—Dated April 1st, 1943, of The Cleveland, Cincinnati, Chicago and St. Louis Railway Co., *et al.*, for Appointment of Special Master (R. 14)

IN THE
DISTRICT COURT OF THE UNITED STATES
FOR THE SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

The Petition of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, hereinafter called the Big Four, and of The New York Central Railroad Company, hereinafter called the New York Central, respectfully shows and alleges:

1. That The Peoria and Eastern Railway Company, hereinafter called the Peoria and Eastern, is a railroad corporation of the State of Illinois and owns a line of railroad extending westward from the boundary line between the States of Illinois and Indiana to Pekin in the State of Illinois (called the Illinois part of its line) and owns or has a leasehold interest in a line of railroad extending from the boundary line between the States of Illinois and Indiana to the tracks of the Indianapolis Union Railway Company at or near Indianapolis in the State of Indiana (called the Indiana part of its line).

2. That on April 1, 1940, there became due and payable by the Peoria and Eastern:

> $846,000, principal amount, of the Preferred Bonds of The Indiana, Bloomington and Western Railway Company secured by a prior lien upon a portion of the railroad of the Peoria and Eastern,

$500,000, principal amount, of indebtedness of the Peoria and Eastern incurred to pay the Preferred Bonds of The Ohio, Indiana and Western Railway Company which matured on April 1, 1938, and were secured by a prior lien upon a portion of the railroad of the Peoria and Eastern, and

$8,876,000, principal amount, of the First Consolidated Mortgage Bonds of the Peoria and Eastern.

That on said date the term of the Operating Agreement pursuant to which the lines of railroad of the Peoria and Eastern had been operated by the Big Four or New York Central, as lessee of the Big Four, likewise was to expire, subject to the right of the Big Four, at its election, to extend the said agreement for a further term.

3. That on April 1, 1940, there also became enforceable the so-called Purchase Money Lien for $5,000,000 declared and reserved in a deed of a line of railroad extending from Indianapolis, Indiana, to Springfield, Ohio, made by Charles H. Coster and Samuel Spencer to the Big Four, which Purchase Money Lien was pledged under the First Consolidated Mortgage of the Peoria and Eastern, and subject to such prior pledge, under the Income Mortgage of the Peoria and Eastern, and subject to such prior pledges was assigned to the Peoria and Eastern.

4. That on March 29, 1940, the Peoria and Eastern, following entry of an order by the Interstate Commerce Commission under Section 20a of the Interstate Commerce Act containing the special findings provided for in said Chapter XV of the Bankruptcy Act, and the assents to the Plan required by said Chapter having been obtained, filed in the Office of the Clerk of this Court a Petition averring

that it was unable to meet its debts as they matured or were about to mature and that it desired to carry out a plan of adjustment pursuant to Chapter XV of the Bankruptcy Act; that said Plan of Adjustment contemplated the payment of the so-called Purchase Money Lien of $5,000,000 by the Big Four, the application of the moneys arising from such payment in the satisfaction of the two issues of prior lien bonds above mentioned (the Preferred Bonds of the Indiana, Bloomington and Western and of the Ohio, Indiana and Western) or of indebtedness incurred in connection with such satisfaction, and to the reduction pro rata of the principal amount of the First Consolidated Mortgage Bonds of the Peoria and Eastern and the extension for twenty years of the maturity date of the principal remaining unpaid of such bonds after such reduction, and the guaranty of the payment of the interest on the remaining principal of such First Consolidated Mortgage Bonds during such extended term by the extension for twenty years of the Operating Agreement under which the railroad of the Peoria and Eastern was operated by the Big Four, or the New York Central as lessee of the Big Four as aforesaid.

5. That following the filing of such Petition this Special Court was convened in the manner provided by Section 266, as amended, of the Judicial Code, and following a hearing the Special Court entered its order dated March 29, 1940, approving the Petition as properly filed under said Chapter XV of the Bankruptcy Act and fixing a date for a hearing; that pursuant to said order and notices given pursuant thereto, public hearings were held by the Special Court, and on July 8, 1940, the Special Court filed its opinion, all the Judges concurring, setting forth the conclusions

of the Court and the reasons therefor and holding that the Plan of Adjustment should be modified so as to provide that the Income Bondholders, so long as any of the Income Bonds of the Peoria and Eastern remained unpaid, should have one Director upon the Board of Directors of the Peoria and Eastern, and that with such modification the Plan complied with and satisfied the requirements of Chapter XV of the Bankruptcy Act and should be approved and confirmed.

6. That by Decree dated July 23, 1940, the Special Court confirmed the Plan of Adjustment as modified as aforesaid, and pursuant to said Decree the Plan became effective and the payments and adjustments provided for in said Plan were duly made and the instruments required to be executed pursuant to said Plan were duly executed and delivered.

7. That in said Decree (Section 20) the Special Court reserved full jurisdiction to correct or perfect the Decree, to take any other or further action in aid of said Decree, to consider and act upon all matters dealt with in any report made relating to the effectuation of the Plan as modified and the Decree and otherwise to take all such supplementary action as the Court might deem proper in the premises, provided that no action taken should impose or result in, any liability on anyone for or in respect of any action theretofore taken in accordance with the Decree or any instrument executed pursuant thereto.

8. That Paragraph Third of the Operating Agreement, under which the railroad of the Peoria and Eastern was operated by the Big Four or the New York Central, as lessee of the Big Four, provides as follows:

"The Cleveland Co. is to receive all earnings and income of the use and operation of said 'Indiana part' and of said 'Illinois part' of said line of railroad, and of said rolling stock and equipment, and apply the net earnings of each year arising from the same (to be ascertained by deducting from the earnings and income of the year from its use and operation of said 'Illinois part' and said 'Indiana part,' the expenses of operation and maintenance during such year, including taxes, assessments, insurance, rental and other like charges, and the cost of repairs, renewals and reasonable betterments to the said 'Illinois part' and the said 'Indiana part,' necessary for their economical and efficient operation), together with the net income from the purchase money lien of $5,000,000 on the part of the railroad formerly of the Ohio, Indiana and Western Railway Company between Indianapolis, Indiana, and Springfield, Ohio, to the payment of the interest as and when it shall mature and become payable upon the said two series of bonds, secured by prior mortgages upon said line of railroad, to wit: $1,000,000 of bonds issued by the Indiana, Bloomington and Western Railway Company and $500,000 of Preferred Bonds issued by the Ohio, Indiana and Western Railway Company, and to the payment of the interest as and when it shall become payable upon said First Consolidated Mortgage Bonds of the Peoria Co. After reimbursing itself out of what shall remain of such net earnings and income of the year, not applied as aforesaid to the payment of interest, for any advances hereunder in any previous year remaining unpaid to it (with interest thereon at the rate of six per cent. per annum), the Cleveland Co. shall apply the balance of said net earnings and income to the payment of interest upon said Income Mortgage Bonds according to the requirements of the mortgage securing the same, and pay over to the Peoria Co. any amount

thereof finally remaining. It is understood and agreed that the Cleveland Co. is to be entitled to make the customary charge for the use of any and all additional rolling stock and equipment furnished by it as hereinbefore provided for use on said lines of railroad from time to time, and that such charge shall form part of and be included in the expense of operation hereunder."

9. That in accordance with the provisions of said Plan of Adjustment, said Operating Agreement was extended by an agreement dated as of April 1, 1940, for an additional period of twenty years from April 1, 1940 to April 1, 1960, subject to all the terms, covenants, conditions and agreements contained in the Operating Agreement, except that in view of the payment of the Purchase Money Lien of $5,000,000, therein referred to, and the payment of the Preferred Bonds of The Indiana, Bloomington and Western Railway Company, and the Preferred Bonds of The Ohio, Indiana and Western Railway Company therein referred to, the amount of the deficiency which under the Operating Agreement the Big Four was obligated to provide for and make good in the funds necessary for the due and punctual payment of the interest as it accrued on the two issues of Preferred Bonds above referred to (so paid) and on the First Consolidated Mortgage Bonds of the Peoria and Eastern (so reduced in principal amount and with maturity date extended) and of any tax or taxes which the Peoria and Eastern might be required to pay or retain from the interest on said bonds during such extended term of the Operating Agreement was to be such amount as might be required for the due and punctual payment of the interest as it accrued upon the aggregate principal amount from time to time outstanding of the First Con-

solidated Mortgage Bonds of the Peoria and Eastern not to exceed $4,722,300, principal amount, and of any tax or taxes which the Peoria and Eastern might be required to pay or retain from the interest on said bonds.

10. That at the time of the filing of the Plan of Adjustment, the property of the Peoria and Eastern was also subject to Income Mortgage Bonds in the amount of $4,000,000, which bonds were not affected by the Plan of Adjustment; that Paragraph Sixth of said Income Mortgage provides as follows:

> "That beginning with the year ending December 31, 1890, the Board of Directors of the Railway Company shall ascertain and declare the net earnings and income applicable to the payment of interest upon the bonds secured hereby for the year ending the 31st day of December in each year, by deducting from the gross earnings and income of the Railway Company for such year all interest on prior bonds, and on said First Consolidated Mortgage Bonds, expenses of operation and maintenance, taxes, assessments, insurance, rentals and other like charges, cost of repairs, renewals and reasonable betterments to the property of the Railway Company necessary for its economical and efficient operation, and all deficiencies arising from payments for said purposes in former years not otherwise provided for, and all advances which shall have been made to provide for such deficiencies or any part of them, and shall apply such net earnings and income (or such portion thereof as may be necessary) towards payment of the interest on the bonds hereby secured, in accordance with their terms and the provisions hereof. The said net earnings and income of each year shall be ascertained and declared by the Directors not later than the 1st day of March following each 31st

day of December, and the interest declared by them shall be paid on the first day of April following.

The Railway Company shall on or before the first day of March of each year furnish the trustees with a statement showing the amount of the net earnings and income of the previous year so ascertained and declared to be applicable to the interest on the bonds secured by this mortgage, and give public notice of the rate of interest payable on said bonds. If the trustees shall not be satisfied with the said statement, or if said trustees shall be notified in writing by the holders of bonds to the amount of one-fifth of the amount outstanding that they object to the same within thirty days after the same shall have been received by the trustees, it shall be the duty of the said trustees forthwith to notify the Railway Company of such objection. And the trustees shall have the right to inspect the books of the Railway Company by a proper officer of said Central Trust Company of New York, or by an expert accountant appointed for the purpose (such appointment to be made by said Trust Company so long as it shall continue as one of the trustees hereunder), who shall be paid for his services by the Railway Company.

If the said difference for any reason shall not be adjusted by agreement between the trustees and the Railway Company, or if the trustees be called upon to proceed by the holders of one-fifth of the amount of bonds outstanding secured by this mortgage, who shall also have duly indemnified the trustees against all liability for costs and expenses, then and in that event it shall be lawful for and the duty of the trustees to file a bill in equity against the Railway Company in any court of competent jurisdiction, for an account of the net earnings and income under the provisions of this mortgage, and if

it shall be adjudged in such action that there are such net earnings and income available, under the terms of this mortgage, for the purpose of paying the interest on the bonds secured by this mortgage beyond the amount declared in the statement so furnished by the Railway Company, then, unless the Railway Company shall, within three months after such adjudication, pay the said balance of the net earnings and income so adjudged to be available by way of interest to the holders of the bonds hereby secured, such non-payment shall constitute a default in the payment of interest, for which the trustees shall be authorized to proceed under the terms of the second, third and fourth articles of this mortgage. The remedy herein provided for ascertaining the amount of the net earnings, in case of dispute, shall be exclusive of all other proceedings, actions, suits, and demands whatsoever."

That annual statements pursuant to the provisions of the Income Mortgage have been furnished by the Peoria and Eastern annually and that no objection to the annual statements so furnished has ever been made pursuant to the above provision.

11. That at the time of the entry of the Decree approving the Plan of Adjustment of the Peoria and Eastern as aforesaid, the Peoria and Eastern was indebted and at the present time is indebted to the Big Four and to the New York Central in certain amounts representing advances made by the Big Four and the New York Central pursuant to the terms of the Operating Agreement to make up the deficiency in the funds of the Peoria and Eastern necessary to pay the amounts provided to be paid under the above mentioned Paragraph Third of the Operating Agreement

on account of the interest on the prior bonds and First Consolidated Mortgage Bonds; that the amount of said indebtedness which has not been reimbursed as shown upon the books of the Peoria and Eastern was as of April 1, 1940, $1,160,153.89 as to the Big Four, and $1,422,389.37 as to the New York Central; that the amount of said indebtedness which has not been reimbursed as shown upon the books of the Peoria and Eastern was as of December 31, 1942, $1,158,173.12 as to the Big Four, and $1,198,514.21 as to the New York Central.

12. That pursuant to the requirement of the Decree approving the Plan of Adjustment, an agreement was entered into among the Peoria and Eastern, the Big Four and New York Central, which agreement was approved by the Special Court in its Order Supplemental to Decree dated April 29th, 1941, providing the procedure for the nomination by the Income Bondholders of a Director to represent the Income Bondholders upon the Board of Directors of the Peoria and Eastern, and pursuant to the procedure provided for in said agreement, John W. McInerney was duly nominated as the representative of the Income Bondholders upon the Board of Directors of the Peoria and Eastern, and following such nomination duly elected.

13. That the Special Court in its Order Supplemental to Decree dated April 29th, 1941, provided in Section 24 of the Decree, as amended, as follows:

> "All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Peti-

tioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', *upon objection by the representative of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so.*"

14. That at the meeting of the Board of Directors of the Peoria and Eastern held on the 24th day of February, 1943, John W. McInerney, the representative of the Income Bondholders upon the Board of Directors of the Peoria and Eastern, having made objection to that portion of the accounts of the Peoria and Eastern for the year 1942 which provided for the reimbursement to the New York Central on account of the indebtedness owing to it as aforesaid, of the sum of $469,889.27, which sum was available for reimbursement of a portion of the principal and interest owing from the Peoria and Eastern to the New York Central on account of the so-called inter-company accounts between the Big Four, the New York Central on the one hand, and the Peoria and Eastern on the other, and following such objection the following action was taken by the Board of Directors of the Peoria and Eastern:

"The President stated that the representative of the Income Bondholders on the Board had made objection to the crediting to the operating companies

of the amount of the net surplus shown in statement of Earnings, Expenses, and Deductions from Income for the year ended December 31, 1942, approved at this meeting.

Whereupon, the following was presented and, on motion, unanimously adopted:

RESOLVED: That in conformity to section 24 of the Decree entered July 29, 1940, in the United States District Court for the Southern District of New York, as modified by Supplemental Decree dated April 9, 1941, the amount of net surplus shown in the statement of Earnings, Expenses and Deductions from Income for the year ended December 31, 1942, approved at this meeting be not presently credited to the operating companies or either of them, but be held in suspense until they prove or establish their right to have the same so credited in accordance with the decree."

Petitioners therefore respectfully pray that an order be entered by the Special Court appointing a Special Master to hear and report to the Special Court his findings and conclusions as to the amount and validity of the inter-company accounts between the Big Four and New York Central and the Peoria and Eastern, to the intent that said inter-company accounts as referred to in Section 24 of the Order Supplemental to Decree entered in the above entitled proceeding may be settled and stated by the Special Court and the right of the petitioners to have the said amount of $469,889.27 applied in reduction of the indebtedness of the Peoria and Eastern to them as shown by said inter-company accounts as so settled and stated may be proved and established and following the statement of such accounts that such modification be made in Section 24 of the Order

Supplemental to Decree as may be just and proper in the premises.

Dated, New York, April 1st, 1943.

THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY,

By W. F. PLACE,
Vice President.

THE NEW YORK CENTRAL RAILROAD COMPANY,

By W. F. PLACE,
Vice President.

State of New York, }
County of New York, } ss.:

WILLARD F. PLACE makes solemn oath that he is a Vice President of The Cleveland, Cincinnati, Chicago and St. Louis Railway Co., and of The New York Central Railroad Company, named as Petitioners in the foregoing Petition, and is duly authorized to make said petition and this affidavit in their behalf, and that the statements contained in said petition are true according to the best of his knowledge, information, and belief.

W. F. PLACE

Subscribed and sworn to before
me this 1st day of April, 1943.

WM. F. McGINN
Notary Public, Westchester County
Cert. filed in N. Y. Co. No. 101, Reg. No. 71 Mc 5
Commission expires March 30, 1945

ORDER OF THE DISTRICT COURT—Dated May 21, 1943, Appointing Special Master, and Appointing Charles S. Aronstam as Counsel to Represent the Income Bondholders (R. 16)

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

ORDER

Upon due consideration of the petition of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company and The New York Central Railroad Company, verified the 1st day of April, 1943, and the Notice of Motion, dated April 1st, 1943, for an order appointing a Special Master to hear and report his findings and conclusions with respect to the amount and validity of the accounts between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, The New York Central Railroad Company and The Peoria and Eastern Railway Company; and of the answer of the Income Bondholders' Protective Committee for The Peoria and Eastern Railway Company, verified the 6th day of April, 1943, joining in said application, and

This motion having come on for hearing on April 7th, 1943 and counsel for the First Mortgage Bondholders' Committee and for Central Hanover Bank and Trust Company appearing but not opposing said motion; and the motion having been submitted to this Court; and the Court being fully advised in the premises and having filed its decision herein dated April 14th, 1943, it is

Order of Reference—May 21, 1943

ORDERED that the motion be, and is hereby, in all respects granted, and it is further

ORDERED that FRANCIS H. HORAN, Esq. of New York City be and is hereby appointed Special Master to hear and report to the Court his findings and conclusions as to the amount and validity of the inter-company accounts between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, The New York Central Railroad Company and The Peoria and Eastern Railway Company arising from the operation of The Peoria and Eastern Railway Company by The New York Central Railroad Company and The Cleveland, Cincinnati, Chicago and St. Louis Railway Company under the Operating Agreement between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company and The Peoria and Eastern Railway Company, dated February 22nd, 1890, and the Agreement in Renewal thereof made and executed April 1st, 1940, to the end that said inter-company accounts, as referred to in Section 24 of the Order Supplemental to Decree entered in the above entitled proceedings on April 1st, 1941, may be settled and stated by this Court, and it is further

ORDERED that Charles S. Aronstam, counsel for the Income Bondholders' Protective Committee be and is hereby designated as counsel to represent the Income Bondholders of The Peoria and Eastern Railway Company in these proceedings before the Special Master, and that the said counsel with the approval of the Special Master may employ accountants and traffic experts to assist him in connection therewith, and it is further

ORDERED that the compensation of Charles S. Aronstam as counsel for the Income Bondholders and of the

accountants and traffic experts, together with the necessary disbursements of said representation, shall be approved and determined by the Court.

Dated New York, N. Y. May 21, 1943.

LEARNED HAND
U. S. Circuit Judge

WOOLSEY
U. S. District Judge

HULBERT
U. S. District Judge

PETITION—Dated June 24, 1943, of The Peoria and Eastern Railway Company, for Approval of Retainer of Counsel (R. 17)

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

The Petition of The Peoria and Eastern Railway Company respectfully shows and alleges:

1. On or about the 7th day of April, 1943, The Cleveland, Cincinnati, Chicago and St. Louis Railway Company

and The New York Central Railroad Company filed herein a Petition and Motion for an order appointing a Special Master to hear and report to the Special Court his findings and conclusions as to the amount and validity of the inter-company accounts between the Big Four and New York Central and The Peoria and Eastern, to the intent that said inter-company accounts, as referred to in Section 24 of the Order Supplemental to Decree, entered in the above-entitled action on April 29th, 1941, might be settled and stated by the Special Court.

2. The Income Bondholders' Protective Committee for The Peoria and Eastern Railway Company interposed an answer to the said Petition and joined in the prayer for the appointment of a Special Master.

3. On April 14, 1943, the Special Court filed its decision granting said Motion for the appointment of a Special Master, and requiring submission of proposed orders on Notice.

4. Thereafter, the Big Four and New York Central submitted their proposed order, and the Income Bondholders' Protective Committee submitted a proposed counter order. The counter order submitted by the Income Bondholders' Protective Committee provided for the designation of the Special Master, and further decreed that Charles S. Aronstam, counsel for the Income Bondholders' Protective Committee, be designated as counsel to represent the Income Bondholders' Protective Committee of The Peoria and Eastern Railway Company in these proceedings before the Special Master. It further provided that the compensation of Charles S. Aronstam, as counsel for the

Income Bondholders' Protective Committee, together with necessary disbursements, should be borne and paid by The Peoria and Eastern Railway Company in such amounts as should be approved and determined by the Court. The Court signed this order, first striking out the provision for payment of counsel fees and disbursements by The Peoria and Eastern Railway Company.

5. In the Memorandum submitted by the Big Four and New York Central in support of their proposed order for the appointment of a Special Master in this proceeding, it was stated that in view of the relationship existing between the New York Central and the Peoria and Eastern, the latter company was considering the employment of counsel independent of the New York Central to represent it therein and that if and when such counsel was retained a full statement of such engagement would be made to the Court for such approval or consideration as might be appropriate.

The Peoria and Eastern has, subject to the approval of the Court, arranged to retain Frank W. H. Adams, Esq., a member of the firm of Dorsey, Adams and Walker of 44 Wall Street, New York City, to represent it in this proceeding, with the understanding that Mr. Adams will to the best of his ability as an attorney protect the interest of the Peoria and Eastern therein, that the Big Four and the New York Central will upon request furnish to Mr. Adams any information relevant to said inter-company accounts in their possession which he may wish to submit to the Special Master, and that Mr. Adams will look only to the best interest of the Peoria and Eastern without regard to any stock or other control that the Big Four or

New York Central may have of the Peoria and Eastern. In order that Mr. Adams may be free from any obligation to the New York Central or Big Four as controlling stockholder of the Peoria and Eastern with respect to his fees, it has been agreed, subject to the approval of the Court, that the fees for the services to be performed by Mr. Adams in this proceeding shall be Five Thousand ($5,000) Dollars and shall be paid to him by the Peoria and Eastern, provided, however, that if these proceedings are extended the Peoria and Eastern is to consider the question of additional compensation with the independent counsel subject to the approval of the Court.

WHEREFORE, in accordance with the Memorandum above referred to, the foregoing statement as to the proposed retainer of Mr. Adams to represent the Peoria and Eastern is submitted to the Court for such approval or instructions as may be appropriate.

THE PEORIA AND EASTERN RAILWAY COMPANY

By W. F. PLACE
Vice President

Petition—June 24, 1943

State of New York, }
County of New York, } ss.:

WILLARD F. PLACE makes solemn oath that he is a Vice President of The Peoria and Eastern Railway Company, named as Petitioner in the foregoing Petition, and is duly authorized to make said petition and this affidavit in its behalf, and that the statements contained in said petition are true according to the best of his knowledge, information, and belief.

W. F. PLACE

Subscribed and sworn to before
me this 24th day of June, 1943.

LISLE O. WAGNER
Notary Public, Westchester County
Certificate filed in New York Co.
N. Y. Co. Clk's No. 509, Reg. No. 306-W-5
Commission Expires March 30, 1945

(SEAL)

ORDER OF DISTRICT COURT—Dated July 2, 1943, Approving Appointment of Frank W. H. Adams, Esq., as Counsel for The Peoria and Eastern Railway Company (R. 19)

UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

Before:

L. HAND and HULBERT, *JJ.*

This cause came on to be further heard at the June, 1943 term of this court, and thereupon, upon consideration thereof, it is

ORDERED, ADJUDGED and DECREED, that the appointment by The Peoria and Eastern Railway Company, of Frank W. H. Adams, Esq. to represent it in the accounting proceeding now before Francis H. Horan, Esq., Special Master, be, and the same hereby is approved, without however, approving the arrangement for the payment of the fees of the said Adams, which shall be determined by the court after the conclusion of the proceeding.

Dated: New York, July 2, 1943.

LEARNED HAND
United States Circuit Judge.

HULBERT
United States District Judge.

PLAN OF ADJUSTMENT—Dated January 10, 1940, of The Peoria and Eastern Railway Company (R. 1)

THE PEORIA AND EASTERN RAILWAY COMPANY

PLAN OF ADJUSTMENT UNDER CHAPTER XV OF THE BANKRUPTCY ACT

Dated January 10, 1940.

In Respect of the Extension of the Date of Maturity from April 1, 1940 to April 1, 1960 of a Part of the Principal

OF

THE PEORIA AND EASTERN RAILWAY COMPANY'S
FIRST CONSOLIDATED MORTGAGE BONDS,
DATED FEBRUARY 22, 1890.

ARTICLE I—Introductory Statement, Pages 2 to 16 hereof.

ARTICLE II—Statement of the present situation of the Peoria and Eastern as to bond maturities, etc., Pages 16 to 18 hereof.

ARTICLE III—Proposed Plan of Adjustment, Pages 18 to 23 hereof.

ARTICLE IV—Method of assent to the Plan, Pages 23 to 24 hereof.

ARTICLE V—Withdrawals and effective date of Plan, Pages 24 to 27 hereof.

ARTICLE VI—Notices, Page 27 hereof.

Form of Certificate of Deposit, Pages 28 to 30.

Results of Operation, Corporate Income Account, Profit and Loss Account and Condensed General Balance Sheet, Pages 31 to 33.

* * * * * * *

III.

PROPOSED PLAN OF ADJUSTMENT.

1. The Big Four has agreed that, if the proposed Plan of Adjustment herein provided for shall become effective, it will pay over to the Central Hanover Bank and Trust Company, as Trustee under the First Consolidated Mortgage and, subject to the prior lien of the First Consolidated Mortgage, as Trustee under the Income Mortgage, the sum of $5,000,000 in full satisfaction of the Purchase Money Lien on the Springfield Division (declared and reserved under the deed to the Big Four dated February 22, 1890). The Peoria and Eastern, the Trustee under the First Consolidated Mortgage, and the Trustee under the Income Mortgage upon such payment are to give such acquittances to the Big Four as may be appropriate to free the Springfield Division from such Purchase Money Lien.

2. The sum of $5,000,000 to be paid in satisfaction of the Purchase Money Lien on the Springfield Division, upon its payment, is to be applied as follows:

(a) The sum of $846,000 to the payment of the principal of the outstanding Preferred Bonds of The Indiana, Bloomington and Western Railway Company, originally in the aggregate principal amount of $1,000,000, of which $846,000, principal amount, are now outstanding, and following such payment the mortgage of The Indiana, Bloomington and Western Railway Company securing such bonds to be satisfied and discharged of record; the $846,000 principal amount of such bonds now outstanding, the principal amount of such bonds now held in the Treasury of the Peoria and Eastern and the $124,000 principal amount of First Consolidated Mortgage Bonds of the Peoria and Eastern now held in the Sinking Fund for such bonds to be cancelled;

(b) The sum of $384,500 on account of the First Consolidated Mortgage Bonds of the Peoria and Eastern pledged by the Peoria and Eastern as part collateral security for its promissory note in the amount of $500,000 held by The Securities Corporation of the New York Central Railroad and secured by First Consolidated Mortgage Bonds in the amount of $500,000 (issued on April 1, 1938 in exchange for the Prior Bonds of The Ohio, Indiana and Western Railway Company maturing on that date and such note having been given to obtain the moneys necessary to pay such maturing Prior Bonds) and upon such payment $290,000, principal amount, of such bonds are to be released from such pledge and cancelled and the sum of $94,500 is to be paid on account of the principal of the $210,000, principal amount, of the remaining bonds so pledged (on the basis of $450.00 for each $1,000 bond), reducing the amount unpaid on account of the principal amount of such remaining bonds to $115,500.

Upon the proposed Plan of Adjustment becoming effective, The Securities Corporation of the New York Central Railroad, the holder of the above mentioned note for $500,000, has agreed to accept said sum of $384,500 and said $115,500, principal amount, of First Consolidated Mortgage Bonds as reduced as aforesaid and to be extended as provided in Paragraph 3 below in payment of said note for $500,000, thus enabling a payment of $450.00 to be made on each $1,000 of the remaining outstanding First Consolidated Mortgage Bonds of the Peoria and Eastern and also securing the release from pledge under said note of the Peoria and Eastern's holdings of stock in the Peoria and Pekin Union Railway Company now pledged as part of the collateral for such note.

(c) The sum of $3,769,200 ratably on account of the principal of the remaining $8,376,000, principal amount, of First Consolidated Mortgage Bonds, being at the rate of $450.00 for each $1,000 bond, reducing the amount unpaid on account of the principal amount of such remaining bonds to $4,606,800.

(d) The sum of $300 remaining of said $5,000,000 to be paid in satisfaction of the Purchase Money Lien after the payments provided for in subdivisions (a), (b) and (c) above, is to be paid over to the Trustee under the First Consolidated Mortgage and applied by such Trustee in the purchase in the market at the lowest price obtainable, not in excess of the principal amount and accrued interest (which interest shall be paid by the Peoria and Eastern to the Trustee upon request therefor) of First Consolidated Mortgage Bonds which shall have been reduced in principal amount and the maturity date extended as provided in the Plan (or bonds issuable in exchange therefor under the Supplemental Inden-

ture herein provided for); the bonds so purchased by the Trustee shall, following such purchase, be cancelled.

3. The date of maturity of the portion unpaid of the principal of the First Consolidated Mortgage Bonds (after the payments provided for in subdivisions (b) and (c) above), aggregating $4,722,300, is to be extended, without impairment of the lien of the mortgage securing such bonds (but with the Purchase Money Lien discharged by payment as provided in 2 above), from April 1, 1940 to April 1, 1960, such extended bonds to continue to bear interest during the period of their extension at the present rate of 4% per annum, payable semi-annually.

4. The Peoria and Eastern, upon the Plan of Adjustment becoming effective, is to enter into an appropriate supplemental indenture with the Central Hanover Bank and Trust Company as Trustee under the First Consolidated Mortgage providing:

(a) For the application of the moneys received on account of the payment of the Purchase Money Lien to the purposes specified in subdivisions (a), (b), (c) and (d) of Section 2 above;

(b) For the extension of the date of maturity of the First Consolidated Mortgage Bonds (as reduced in principal amount under the payments provided for in subdivisions (b) and (c) of Section 2 above) from April 1, 1940 to April 1, 1960, with interest on the reduced principal amount thereof at the rate of 4% per annum, payable semi-annually April 1 and October 1;

(c) For the continuing security of the First Consolidated Mortgage in respect of the First Con-

solidated Mortgage Bonds as so modified (including the $50, $500 and $1,000 bonds to be issuable for purposes of exchange as referred to in (f) below);

(d) For the pledging under the First Consolidated Mortgage, of the Peoria and Eastern's holdings of stock of the Peoria and Pekin Union Railway Company (subject to necessary consents to such pledge being obtained from the other stockholders of that company and to the restrictions imposed in any such consents);

(e) For the placing of appropriate notations upon such Bonds showing the reduction in the principal amount thereof and the extension of the date of maturity of the unpaid principal amount from April 1, 1940 to April 1, 1960, with interest at 4% per annum payable semi-annually and for other appropriate action in connection therewith;

(f) For the exchangeability of such Bonds as so modified, without expense to the bondholders, for an equal principal amount of bonds of the denominations of $50, $500 and $1,000, with coupons covering the semi-annual installments of interest, payable October 1, 1940 to April 1, 1960, attached, to be issued under the First Consolidated Mortgage as to be provided in such supplemental indenture; such bonds of the denominations of $50 and $500 to be exchangeable for like aggregate principal amounts of bonds of such larger denominations upon the payment of charges, all as to be provided in the supplemental indenture.

NOTE. The Peoria and Eastern, if the Plan becomes effective, will make application for the listing of such Bonds in the denominations of $500 and $1,000 on the New York Stock Exchange.

5. The Big Four with the approval of the New York Central, as lessee, has elected, subject to the required authorization and approval of governmental authorities, to continue to operate the properties of the Peoria and Eastern and upon such authorization being obtained and upon the Plan becoming effective is to enter into an agreement with the Peoria and Eastern evidencing such election for the period from April 1, 1940 to April 1, 1960, upon the terms contained in the Operating Agreement, except that by reason of the payment by the Big Four of the $5,000,000 Purchase Money Lien, the payment of the Prior Bonds, and the reduction in principal of the First Consolidated Mortgage Bonds, the annual amount which the Big Four during such extended term of the Operating Agreement shall be obligated under such Operating Agreement to make available for the payment of interest shall be reduced to such amount as may be required during such extended term to pay the interest on the First Consolidated Mortgage Bonds with principal amount reduced and extended, pursuant to the Plan of Adjustment.

6. The Big Four has agreed that if the proposed Plan of Adjustment becomes effective it will replace or cause to be replaced, equipment of the Peoria and Eastern which has been retired and not replaced or has become unserviceable for further use with suitable equipment, or additions and betterments to equipment, equal in value to the cost to the Peoria and Eastern of such retired or unserviceable equipment as the same appears upon the books of the Peoria and Eastern, and that during the extended term of the Operating Agreement it will replace annually any equipment which may, during such year,

have been retired or become unserviceable for further use, with suitable equipment, or additions and betterments to equipment, equal in value to the cost to the Peoria and Eastern of such retired or unserviceable equipment, as the same appears upon the books of the Peoria and Eastern; all expenditure therefor, shall, however, be charged against the balance remaining at the time in the equipment retirement account held for the Peoria and Eastern.

7. The advances which have been made by the Big Four and the New York Central to the Peoria and Eastern under the Operating Agreement (amounting as of November 30, 1939 to $2,506,192) shall continue their existing status under the Operating Agreement during the extended term of such Agreement.

8. The holders of the Income Mortgage Bonds of the Peoria and Eastern to continue their status under the Income Mortgage (with the Purchase Money Lien discharged by payment and the amount of bonds prior thereto reduced as provided in the Plan), subject to the First Consolidated Mortgage Bonds as modified and extended pursuant to the Plan and to the Operating Agreement as extended pursuant to the Plan.

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FINDINGS OF FACT OF DISTRICT COURT— Dated July 23, 1940 (R. 6)

IN THE

DISTRICT COURT OF THE UNITED STATES

FOR THE SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

THE COURT HEREBY MAKES THE FOLLOWING FINDINGS:

1. Petitioner is a railroad corporation organized and existing under the laws of the State of Illinois with certificate of incorporation, dated February 20, 1890. Pursuant to action of the stockholders of the Peoria and Eastern at a meeting held on the 14th day of February, 1940, the charter of Petitioner was renewed and extended for the period of fifty years from February 20, 1940.

2. Petitioner is a carrier by railroad, as defined in Section 20a of the Interstate Commerce Act, organized for the purpose of engaging in transportation of persons and property in interstate commerce pursuant to Part 1 of the Interstate Commerce Act, and is not now and has not been within ten years prior to the filing of the Petition herein, in equity receivership or in proceedings for reorganization under Section 77 of the Bankruptcy Act.

3. Petitioner is the owner of a line of railroad extending from a connection with the tracks of the Peoria and Pekin Union Railway Company at or near Peoria, Illinois, eastward to the Illinois-Indiana boundary line and is the

lessee in perpetuity (with ownership of the reversion, but without merger or absorption of the leasehold interest or impairment of any existing transfer or assignment or mortgage thereof) of a line of railroad extending from the Illinois-Indiana boundary line to the tracks of the Indianapolis Union Railway at or near Indianapolis, the distance of both lines totalling approximately 201.53 miles. There are a total of fifty cities and villages along the railway, having a population of 613,954.

4. During the period of more than six months preceding the filing of the Petition herein, Petitioner has had and now has its principal executive office in the Borough of Manhattan, City and State of New York, and such office is within the territorial jurisdiction of this Court.

5. By deed dated February 21, 1890, William P. Fishback and Benjamin R. Cowen, as Special Master Commissioners, in accordance with decrees entered in the Federal Circuit Courts having jurisdiction of the foreclosure of The Ohio, Indiana and Western Railway Company, together with The Ohio, Indiana and Western Railway Company, conveyed to Charles H. Coster and Samuel Spencer, as joint tenants, for the consideration of $3,000,000, the Ohio, Indiana and Western Railway extending from the City of Pekin, Illinois, to the City of Springfield, Ohio, subject to the lien of:

(a) The mortgage of The Indiana, Bloomington and Western Railway Company dated April 15, 1879, securing $1,000,000, principal amount of its 7% Preferred Bonds upon that portion of the former Ohio, Indiana and Western Railway extending from Pekin, Illinois, to Indianapolis, Indiana. Said bonds, here-

inafter called the I. B. & W. Bonds, matured January 10, 1900, and the time of payment thereof was by agreement dated August 1, 1898, extended to April 1, 1940, with the rate of interest reduced to 4% per annum;

(b) The mortgage of The Ohio, Indiana and Western Railway Company dated April 2, 1888, securing $500,000, principal amount of its 5% Preferred Bonds maturing April 1, 1938, upon the former Ohio, Indiana and Western Railway from Pekin, Illinois, to Springfield, Ohio. Such bonds are hereinafter called the O. I. & W. Bonds, and the I. B. & W. Bonds and the O. I. & W. Bonds are collectively hereinafter called the Prior Bonds.

6. By deed dated February 22, 1890, Charles H. Coster and Samuel Spencer, for the consideration of $5,000,000, to be paid as provided in said deed, conveyed to The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, hereinafter called the Big Four, that portion, hereinafter called the Springfield Division, of the former Ohio, Indiana and Western Railway extending from Springfield, Ohio, to the tracks of the Indianapolis Union Railway Company in or near Indianapolis, excepting therefrom the engines, cars, rolling stock and supplies. By said deed the Big Four agreed to use and operate said railroad and to pay to the grantors, their successors and assigns, as interest on the said sum of $5,000,000, the net income arising from the use and operation of the railroad not to exceed the sum of $200,000 in any one year. It was further provided that in the absence of default on the part of the Big Four said sum of $5,000,000 was not to become due and payable until the expiration of fifty years from April 1, 1890, unless the Big Four should elect sooner to pay the same, but in case of

default continuing for thirty days, or in case of default in the payment of said sum of $5,000,000 at the expiration of fifty years, the grantors were authorized to take proceedings for the enforcement of said Lien. Nothing contained in the deed was, however, to be taken as implying any covenant on the part of the Big Four to pay said sum of $5,000,000, the intent, as declared in the deed, being that the grantors relied solely upon the security of the property conveyed for the payment of the purchase money of $5,000,000 and should retain a lien therefor.

7. By deed dated February 22, 1890, Charles H. Coster and Samuel Spencer, in consideration of the delivery of $7,930,000, principal amount of First Consolidated Mortgage Bonds, $4,000,000, principal amount of Income Bonds, and $9,999,500, par value of the capital stock of Petitioner, disposed of portions of the former Ohio, Indiana and Western Railway as follows:

(a) Conveyed to Petitioner all the right, title and interest of the grantors in and to that portion thereof extending from Pekin, Illinois, eastward to the boundary line between the States of Illinois and Indiana, hereinafter called the Illinois portion; and

(b) Leased to Petitioner in perpetuity from April 1, 1890, all their right, title and interest in and to that portion thereof extending from the boundary line between the States of Illinois and Indiana eastward to the tracks of the Indianapolis Union Railway Company in or near Indianapolis, Indiana, hereinafter called the Indiana portion, reserving an annual rental equal to the net earnings, as defined in such deed, of the railway and other property thereby leased, which net earnings, together with the net earnings

derived from the Illinois portion and from the purchase money lien on the Springfield Division reserved in the deed from the grantors to the Big Four, were never to be less than the sum of $412,200 (to be increased $40 for each additional $1,000 of First Consolidated Mortgage Bonds issued in excess of $9,430,000), and Petitioner agreed to pay said rental and to apply the same to the payment of the interest (without deduction for taxes) on the two series of Prior Bonds and on the First Consolidated Mortgage Bonds, and it was agreed that any actual payment of interest should be deemed and taken for all purposes as a satisfaction and discharge of said annual rental for such year to the extent of such payment.

8. By Indenture dated February 22, 1890, hereinafter called the First Consolidated Mortgage, Petitioner mortgaged to the Central Trust Company of New York and Charles W. Fairbanks, as Trustees, to secure an issue of Bonds maturing April 1, 1940, in an aggregate principal sum not in excess of $10,000,000, hereinafter called the First Consolidated Bonds, all the rights of Petitioner then held or thereafter acquired in and to the portion of the former Ohio, Indiana and Western Railway extending from Pekin, Illinois, to the tracks of the Indianapolis Union Railway Company at Indianapolis, subject to the mortgages securing the Prior Bonds, and the Peoria and Eastern in such mortgage agreed to pay the interest on the Prior Bonds and at the maturity thereof to pay the principal of such of the Prior Bonds as shall not meanwhile have been exchanged under the provisions of the mortgage. Petitioner also transferred to the Trustees under the First Consolidated Mortgage all its right, title and interest in and to the $5,000,000 Purchase Money Lien on the Springfield Division

and the income thereof, subject to the prior lien thereon on the mortgage securing the O. I. & W. Bonds. Of the total amount of bonds authorized $7,930,000 were immediately issuable and $1,500,000 were reserved to be issued from time to time for exchange for the Prior Bonds, and it was provided that whenever Petitioner should deliver to the Trustee any of the Prior Bonds either before or after the maturity thereof, together with the unmatured interest coupons thereon, the Trustee would issue to Petitioner or upon its order an amount of reserved bonds equal to the amount of the Prior Bonds so delivered.

9. Petitioner entered into an agreement with the Big Four dated February 22, 1890, and a supplement thereto of even date therewith hereinafter called the Operating Agreement, granting to the Big Four the right to use and operate the Illinois portion and the Indiana portion of the railway of the Petitioner and its rolling stock and equipment during the fifty year period from April 1, 1890, and for such further time thereafter as the Big Four may elect to use and operate said Illinois portion and Indiana portion; and the Big Four agreed to operate the railway of Petitioner during the continuance of the agreement in such manner as to satisfy the requirements of law in respect of Petitioner's railway. In Paragraph First of said agreement the Big Four agreed at its own cost and expense: to furnish all other rolling stock, equipment, labor and supplies; to keep and maintain said line, rolling stock and equipment in good working order; to restore and renew all portions as may be necessary to that end; to pay all taxes on said road, the earnings and income thereof as well as rentals reserved or other like charges; to indemnify and save harmless the Petitioner from any and all claims arising out of its opera-

tion or management; to perform and comply with all and singular the covenants, terms and conditions accepted or undertaken by Petitioner in the conveyances, deeds and leases to it, or in such mortgages given by it to secure its bonds except payment of principal of said bonds or the Prior Bonds. Paragraph Second provided that the Big Four would make good any deficiency which at any time might occur in the fund necessary for due and punctual payment of the accrued interest on the Prior Bonds and of the interest on the First Consolidated Bonds at any time outstanding, after devoting to such payment of interest the net income from the $5,000,000 Purchase Money Lien on the Springfield Division and the net earnings derived from the Illinois portion and Indiana portion, and the Big Four guaranteed that the net earnings and income from said three sources, so actually applied to the payment of said interest, would not be less than $412,200 in each and every year of the fifty years for which it undertook the use and occupation of the Petitioner's railway, such guarantee to be increased $40.00 per year for each $1,000 of First Consolidated Bonds issued in excess of $9,430,000. Paragraph Third provided that the Big Four was to receive all earnings and income from the use and operation of said Illinois portion and Indiana portion and of said rolling stock and equipment and was to apply the net earnings of each year arising from the same (to be ascertained by deducting from the annual earnings and income of said Illinois portion and said Indiana portion the expenses of operation and maintenance during each year, including taxes, assessments, insurance, rental and other like charges, and the cost of repairs, renewals and reasonable betterments to said railway necessary for the economical and efficient operation thereof) together with the net income from the Purchase

Money Lien of $5,000,000 on the Springfield Division, to the payment of interest as and when it shall become payable upon the Prior Bonds, and to the payment of interest as and when it shall become payable upon the First Consolidated Bonds. The Big Four was to reimburse itself out of what remained of such net earnings and income, not applied as aforesaid to the payment of interest, for any advances made under the Operating Agreement in any previous year remaining unpaid to it (with interest at the rate of 6% per annum); and was to apply the balance thereof to the payment of interest upon the Income Bonds according to the requirements of the Income Mortgage securing the same, and pay over to the Petitioner any amount finally remaining. The Big Four was entitled to make the customary charge for the use of any and all additional rolling stock and equipment furnished by it for use on said lines of railroad from time to time and such charge was to form part of and be included in the expense of operation thereunder. Paragraph Fifth of the Agreement provided that the Big Four was to look only to such future net earnings of the Petitioner's railway operated by it under the Operating Agreement and the future income from the $5,000,000 Purchase Money Lien on the Springfield Division as should not be required for the payment of interest on the Prior Bonds or the First Consolidated Bonds for the reimbursement to it of any sums it might advance in compliance with the Operating Agreement; and the Petitioner charged all such future net earnings and income, not required for the payment of such interest, with the payment of all such advances with interest as aforesaid.

10. All money provided by the Big Four for interest on the First Consolidated Mortgage Bonds and the Prior

Bonds, over and above the actual net earnings (as defined in Article Third of the Operating Agreement) and the actual net income from the purchase money lien on the Springfield Division, was to be deemed advances against everyone other than the holders of the First Consolidated Mortgage Bonds and the trustees of the mortgage securing the same.

11. By Indenture dated February 22, 1890, made by Petitioner to the Central Trust Company of New York and Charles W. Fairbanks, as Trustees, to secure an issue of bonds maturing April 1, 1990, in the aggregate principal amount of $4,000,000 bearing interest at a rate not in excess of 4% per annum, payable out of the net earnings and income of the Peoria and Eastern as the same should be ascertained for each year, which interest was to be noncumulative, hereinafter called the Income Bonds, Petitioner mortgaged all its rights then held or thereafter acquired in that portion of the former Ohio, Indiana and Western Railway extending from Pekin, Illinois, to the tracks of the Indianapolis Union Railway Company in or near Indianapolis, subject to the two mortgages securing the Prior Bonds aggregating $1,500,000. There was also transferred to the Trustees under the Income Mortgage the rights of Petitioner in the $5,000,000 Purchase Money Lien on the Springfield Division and the income thereof, together with all rights of Petitioner in the premises covered thereby, subject to the prior lien thereon of the mortgage securing the O. I. & W. Bonds. It was provided in the Income Mortgage that the entire railway and property described therein was subject to the further lien thereon, prior and superior to the lien of the Income Mortgage, of the First Consolidated Mortgage and of $10,000,000 of First Consolidated Bonds and of any extension and renewals thereof however

effected, and of the principal and interest of any new series of bonds not exceeding the amount of the First Consolidated Bonds outstanding at the time of such new issue outstanding and bearing interest at no higher rate than 4% per annum and of the mortgage given to secure such new series of bonds, and subject to the right to extend the time of payment of the $5,000,000 Purchase Money Lien on the Springfield Division for the period covered by any such extension of the First Consolidated Bonds or of any new series of bonds and also subject and subordinate to the Operating Agreement. The Income Mortgage further provided that Petitioner should ascertain and declare the net earnings and income applicable to the payment of interest upon the Income Bonds for each year ending December 31 by deducting from the gross earnings and income of Petitioner for such year all interest on the Prior Bonds and on the First Consolidated Bonds, the expenses of operation and maintenance, taxes, assessments, insurance, rentals and other like charges, cost of repairs, renewals and reasonable betterments to the property necessary for its economical and efficient operation, and all deficiencies arising from payments for said purposes in former years not otherwise provided for, and all advances made to provide for such deficiencies and should apply such net earnings and income (or such portion thereof as might be necessary) towards the payment of the interest on the Income Bonds. The amount of such net earnings and income of each year was to be ascertained and declared not later than March 1 following each December 31 and the interest was to be paid on April 1 following. A statement of such net earnings and income was to be furnished to the Trustees annually prior to March 1 and the Trustees were authorized to inspect the

books of Petitioner, and in case of dispute and failure to adjust the differences, the Trustee might bring action for an accounting.

12. By Indenture dated February 22, 1890, Charles H. Coster and Samuel Spencer transferred to the Central Trust Company of New York and Charles W. Fairbanks, all their right, title and interest in and to the Purchase Money Lien on the Springfield Division and in and to the premises conveyed by the deed reserving such lien, upon the trusts and for the uses and purposes declared in the First Consolidated Mortgage and the Income Mortgage, and upon the fulfillment and satisfaction of such trusts, uses and purposes all such right, title and interest was to vest in Petitioner.

13. By Indenture dated March 25, 1890, between Petitioner, the Big Four and the Central Trust Company of New York and Charles W. Fairbanks, as Trustees under the First Consolidated Mortgage and under the Income Mortgage, Petitioner transferred to the Trustees, as trustees of the First Consolidated Mortgage, the covenants on the part of the Big Four contained in Clause Second of the Operating Agreement (summarized above) and all benefits thereof, and the Big Four covenanted and agreed with the Trustees, as trustees under the First Consolidated Mortgage and with all persons who might at any time become holders of First Consolidated Bonds, that it would provide for and make good any deficiency which might at any time occur in the fund necessary for the due and punctual payment as it accrued of the interest on the two series of Prior Bonds and on the First Consolidated Bonds after devoting to such purpose the income from the Purchase Money Lien

and the net earnings from the Illinois portion and Indiana portion of the railway of Petitioner, and further agreed with the Trustees of the First Consolidated Mortgage and of the Income Mortgage that in case of default under either of said mortgages and of proceedings thereunder against the mortgaged premises, the $5,000,000 Purchase Money Lien on the Springfield Division should, at the option of the Trustees, at once become due and enforceable but without liability on the part of the Big Four for the payment of any portion of said sum of $5,000,000.

14. By Indenture dated March 15, 1890, Charles H. Coster and Samuel Spencer quitclaimed to Petitioner all right, title, interest and estate whatsoever then remaining in the grantors in and to the railroad, equipment, property and franchises demised and leased by them to Petitioner under the Indenture dated February 22, 1890, between the Illinois-Indiana boundary line and the tracks of the Indianapolis Union Railway, but without merger or absorption of said leasehold interest or impairment of any existing transfer or assignment or mortgage thereof, and Petitioner declared that such merger or absorption should not take place so long as any such transfer or assignment or a mortgage of such leasehold interest should exist or be in force.

15. In 1919 the Big Four covenanted with the holders of its refunding and improvement mortgage bonds to pay the $5,000,000 Purchase Money Lien on the Springfield Division.

16. Upon the formation of the Petitioner on February 22nd, 1890 the Big Four received, without paying any cash therefor, one-half of the common stock of Petitioner.

17. At or about the same time the Big Four purchased for cash one (1) share of Petitioner's stock and thus became the owner of a majority of the stock of the Petitioner.

18. By reason of its ownership of a majority of the stock of the Petitioner the Big Four and/or the New York Central have completely dominated and controlled the affairs and business of the Petitioner.

19. By lease dated January 2, 1930, the Big Four leased to the New York Central Railroad Company, hereinafter called the New York Central, all its line of railroad and other property, including a transfer of its rights under the Operating Agreement.

20. The railway of Petitioner primarily serves an agricultural territory, and is therefor susceptible to ups and downs in its revenues due to the recurring droughts and short grain crops in Indiana and Illinois. It runs through a territory subject to substantial truck competition as well as competition with such east and west railroad lines as the Pennsylvania, Nickel Plate, Toledo, Peoria and Western, and the Chicago and Alton. During the period January 1, 1930 to September 30, 1939, the Peoria and Eastern handled on the average about 60,000 loaded cars and 2,000,000 tons of freight per year.

21. Of the total traffic handled over the railway of Petitioner during the period January 1, 1930 to September 30, 1939, 9.9 per cent originated and terminated on its line; 16.9 per cent originated on its line and was delivered by it to connecting railroads; 20.3 per cent was received by it from connecting railroads and terminated on its line; and

52.9 per cent was what is called overhead traffic, that is received by it from and delivered by it to connecting railroads.

22. The New York Central and the Big Four had at all times since the inception of Petitioner enjoyed unrestricted control over the solicitation of traffic on Petitioner's property.

23. A considerable volume of business originating on the Peoria and Eastern finds its market on the New York Central Lines. Similarly, a large portion of the total traffic of the Peoria and Eastern comes to it from the New York Central. Of the loaded cars received by the Peoria and Eastern from connecting railroads, on the basis of a study of the month of October, 1936 (which month was deemed representative by the operating and traffic officers), 74% was delivered to it by the New York Central, and of the loaded cars delivered by the Peoria & Eastern to connecting railroads, 41% was delivered by it to the New York Central.

24. Upon the basis of the continued operation of the railway of Petitioner by the New York Central under the Operating Agreement as extended, it is estimated that, assuming the continuance of the general basis of earnings and expenses which prevailed in 1939, Petitioner should show a corporate income for 1940 of about $304,727 before fixed charges. The income would be increased were there to be an increase in freight revenues.

25. The above estimate is, however, based upon the continuance of the operation of the railway of Petitioner by the New York Central and the continuance of the routing of the volume of traffic now routed over the railway of Peti-

tioner by the New York Central. Were the existing arrangement under which the New York Central operates the railway of Petitioner as part of the New York Central System to be interrupted, so that any substantial portion of the 74% of the connecting line traffic which is now routed by the New York Central over Petitioner's railway to be routed over another line between Indianapolis and Peoria, it is impossible to say what the income of Petitioner would be or how it would compare with fixed charges. Were the arrangement under which the Springfield Division of the Big Four is now being operated as a part of the Big Four also to be interrupted and the traffic now routed by the New York Central over the Springfield Division to be routed over the other line (slightly longer) which the Big Four now has between Springfield and Indianapolis it is again impossible to say what the income of Petitioner would be from the combined operation of the Peoria and Eastern and of the Springfield Division, or how it would compare with fixed charges.

26. The Springfield Division of the Big Four is the shortest direct route between Springfield, Ohio, and Indianapolis, Indiana. Without the Springfield Division the Big Four would have to reroute its traffic between Springfield and Indianapolis which rerouting would involve additional mileage and increased haulage costs.

27. The advances claimed to have been made by the New York Central and the Big Four, as appears on the books of Petitioner under the heading "Non-Negotiable Debts to the Affiliated Companies", are $2,485,482.58; of said amount $1,806,493.18 represents expenditures for maintenance, additions and betterments; $522,517.24 represents interest ac-

crued on net amount claimed to be due the New York Central and the Big Four; $11,006.02 represents net amount claimed to be due the said companies on account of interest paid on funded debt; and $105,667.37 represents the sinking fund payment made on the Indiana, Bloomington and Western Railway Bonds.

28. According to the petitioner's December 31, 1939 balance sheet the total assets of Petitioner are $27,117,632.68, and the long term debt of Petitioner (including in such class, in addition to the funded debt, the advances claimed to have been made by the Big Four and New York Central to Petitioner) is $16,207,482.58. The basic valuation by the Interstate Commerce Commission of the Petitioner's land, road and equipment with net additions and betterments to December 31, 1939, is $10,836,396.86. This figure does not include the Purchase Money Lien of $5,000,000, the equipment retirement account of $516,837.38 and the equipment depreciation account of $773,459.46, and the stock of the Peoria and Pekin Union Railway Company with a par value of $173,000.

29. The New York Central, as lessee of the Big Four, is holding as of December 31, 1939, for the benefit of Petitioner, $516,837.38 in an equipment retirement account and $773,459.46 in an equipment depreciation account and is currently allowing to Petitioner interest at 6% upon such accounts.

30. On April 1, 1938, the O. I. & W. Bonds matured and the mortgage securing such bonds was a lien prior to the lien of the First Consolidated Mortgage upon the property of Petitioner. A 5% promissory note, maturing April 1,

1940, was issued by Petitioner pursuant to the authorization of the Interstate Commerce Commission, secured by $500,000, principal amount of First Consolidated Bonds (issued under the First Consolidated Mortgage in exchange for such maturing O. I. & W. Bonds) and by 1730 shares of the capital stock of the Peoria and Pekin Union Railway Company of a par value of $100 each. Such note was advertised pursuant to the Clayton Act but there being no bidders The Securities Corporation of the New York Central Railroad (all the stock of which is owned by the New York Central) accepted said note at par and provided the funds through which Petitioner was able to meet such maturity of the prior lien bonds on April 1, 1938.

31. On April 1, 1940, the following securities of Petitioner matured:

> $846,000, principal amount of the extended I. B & W. Bonds, originally in the principal amount of $1,000,000, of which $846,000, principal amount are now outstanding and which bonds are secured by a mortgage which is a prior lien upon the property of Petitioner;
>
> $500,000, principal amount evidenced by the promissory note of Petitioner issued to The Securities Corporation of the New York Central Railroad to obtain the moneys necessary to pay at their maturity date, April 1, 1938, the O. I. & W. Bonds in the principal amount of $500,000, which O. I. & W. Bonds were secured by a mortgage prior in lien upon the owned and leased lines of railroad of Petitioner and upon the Springfield Division as well, and which promissory note is secured by $500,000, principal amount of First Consolidated Bonds and 1730 shares of stock of the Peoria and Pekin Union Railway Company;

$8,876,000, principal amount of First Consolidated Bonds of Petitioner (including in such principal amount $500,000 of such bonds pledged as collateral security for the $500,000 promissory note of Petitioner above referred to but excluding $124,000, principal amount of such bonds in the Sinking Fund established in respect of the I. B. & W. Bonds above referred to).

32. On April 1, 1940, there also became enforceable the Purchase Money Lien for $5,000,000 declared and reserved in the deed made by Charles H. Coster and Samuel Spencer to the Big Four of the so-called Springfield Division of the Big Four and which Purchase Money Lien is pledged under the First Consolidated Mortgage of Petitioner and, subject to such prior pledge, under the Income Mortgage of Petitioner, and subject to such pledges is owned by Petitioner.

33. On April 1, 1940, the original fifty-year term of the Operating Agreement under which the owned and leased lines of railroad of Petitioner had been operated by the Big Four from April 1, 1890 to February 1, 1930, and by the New York Central, as lessee of the property of the Big Four, from February 1, 1930, expired; but prior to the expiration thereof the Big Four notified the Peoria and Eastern of its election, in accordance with the terms of said agreement, to extend the same for the further term of twenty years from April 1, 1940 as provided for in the Plan of Adjustment herein referred to.

34. In view of the large amount of securities of Petitioner maturing April 1, 1940, Petitioner was at the time of filing the Petition herein, and continuously thereafter to the date hereof has been, unable to meet its debts, matured or about to mature.

35. On or prior to January 10, 1940, Petitioner prepared a Plan of Adjustment under Chapter XV of the Bankruptcy Act, dated January 10, 1940, in respect of the extension of the date of maturing from April 1, 1940 to April 1, 1960 of a part of the principal of the First Consolidated Bonds of Petitioner, hereinafter called the Plan, a copy of which Plan is attached to and made a part of the Petition filed herein.

36. Thereafter, and on or prior to January 25, 1940, Petitioner secured assurances satisfactory to the Interstate Commerce Commission, hereinafter called the Commission, of the acceptance of the Plan from creditors holding at least 25 per centum of the aggregate amount of all claims affected by the Plan (including all such affected claims against said corporation, its parents and subsidiaries).

37. The Income Bondholders did not receive any notice nor were they represented at the hearings before the Interstate Commerce Commission with respect to the Plan of Adjustment and the renewal of the Operating Agreement. The decision of the Interstate Commerce Commission approving Petitioner's Plan of Adjustment recorded that there was no opposition to the Plan of Adjustment and to the renewal of the Operating Agreement.

38. The Petitioner did not solicit the written consent of the Income Bond Holders to the Plan of Adjustment and the renewal and extension of the Operating Agreement, and such consents were not secured.

39. On March 27, 1940, a report and order were entered by the Commission, upon application of Petitioner, under

Section 20a of the Interstate Commerce Act in Finance Docket No. 12753, a copy of which report and order is attached as Exhibit D to the Petition herein, and was filed with the Petition and made a part thereof. Such report and order of the Commission authorized Petitioner to make the issue or modification of its First Consolidated Bonds as proposed by the Plan (none of the securities of Petitioner being held by or to be issued to the Reconstruction Finance Corporation). Said report and order of the Commission also contained the specific findings required to be made by the Commission under Clauses (a), (b) and (c) of sub-paragraph 2 of the first sentence of Section 710 of the Bankruptcy Act.

40. Thereafter, and prior to the filing of the Petition herein on March 29, 1940, Petitioner secured assents to the Plan by the holders of more than two-thirds of the aggregate principal amount of the First Consolidated Bonds of Petitioner and by The Securities Corporation of the New York Central Railroad.

41. The only claims affected by the Plan and the aggregate amounts thereof are as follows:

> $500,000, principal amount of First Consolidated Bonds securing the 5% promissory note for $500,000, dated March 30, 1938, matured April 1, 1940, made by the Peoria and Eastern to The Securities Corporation of the New York Central Railroad to obtain funds to pay at their maturity, April 1, 1938, the O. I. & W. Bonds and which note is secured by the pledge of $500,000 of First Consolidated Bonds and by 1730 shares of the capital stock of the Peoria and Pekin Union Railway Company. Under the Plan

$290,000, principal amount of such bonds are to be paid in full and cancelled, and $210,000, principal amount of such bonds are to receive a payment of $450 in respect of each $1,000 bond, reducing the principal of each $1,000 bond to $550 and the aggregate principal amount of such bonds to $115,500, and the maturity date of the reduced principal of such bonds is to be extended to April 1, 1960, with interest at the rate of 4% per annum;

$8,376,000, principal amount of First Consolidated Bonds outstanding in the hands of the public, $450 is to be paid on account of the principal of each $1,000 of such bonds, and the maturity date of the reduced principal of such bonds is to be extended to April 1, 1960, with interest at the rate of 4% per annum.

42. The Plan, at the time of the hearings in respect of such Plan, had been accepted by more than three-fourths of the aggregate principal amount of First Consolidated Bonds of Petitioner.

43. The Plan has been accepted in accordance with the requirements of Chapter XV of the Bankruptcy Act.

44. Petitioner is not in need of financial reorganization of the character provided for under Section 77 of the Bankruptcy Act.

45. The inability of Petitioner to meet its debts, matured or about to mature, is reasonably expected to be temporary only.

46. After due consideration of the probable prospective earnings of the property of Petitioner in the light of

of its earnings experience and of such changes as may reasonably be expected, the Plan is in the public interest and in the best interests of each class of creditors and stockholders; is feasible, financially advisable and not likely to be followed by the insolvency of Petitioner or by need of financial reorganization or adjustment; does not provide for fixed charges (of whatsoever nature, including fixed charges on debt, amortization of discount on debt and rent of leased roads) in an amount in excess of what will be adequately covered by the probable earnings available for the payment thereof; leaves adequate means for such future financing as may be requisite; is consistent with adequate maintenance of the property of Petitioner; and is consistent with the proper performance by Petitioner of service to the public as a common carrier, will not impair its ability to perform such service.

47. The Plan, as modified as provided in the Conclusions herein, is fair and equitable as an adjustment, affords due recognition to the rights of each class of creditors and stockholders and fair consideration to each class thereof adversely affected, and will conform to the law of the land regarding the participation of the various classes of creditors and stockholders.

48. The findings set out in Paragraphs 44 to 47, both inclusive, are made by this Court after scrutinizing the facts of record in this proceeding independently of the extent of acceptance of the Plan and of any lack of opposition thereto, and of the fact that the Commission, under Section 20a of the Interstate Commerce Act, has authorized the issuance or modification of securities as

proposed by the plan and of the fact that the Commission has made such or similar findings.

49. Petitioner has not, in connection with the Plan or the effectuation thereof, done any act or failed to perform any duty, which act or failure would be a bar to the discharge of a bankrupt; and the Plan and the acceptances thereof are in good faith and have not been made or procured by any means, promises or acts forbidden by the Bankruptcy Act.

50. The amounts or considerations directly or indirectly paid or to be paid by or for Petitioner for expenses, fees, reimbursement or compensation of any character whatsoever, incurred in connection with the proceeding and Plan or preliminary thereto or in aid thereof, so far as known, are as follows:

Printing and postage	$ 2,200.00
Advertising	1,800.00
Cost of Certificates of Deposit.....	200.00
Trustee's charges in connection with deposit of bonds, issuance of Certificates of Deposit, stamping of bonds, re-issue of bonds, etc.....	12,800.00
Cost of engraving new Bonds.....	7,000.00
Trustee's fees for authenticating new Bonds	2,500.00
Total.....	$26,500.00

All the facts and circumstances relating to the incurring thereof have, after hearings for the purpose, been fully disclosed to this Court, so far as such amounts or considerations could be ascertained at the time of such

hearings; all such amounts or considerations are fair and reasonable and to the extent that any such amounts or considerations are not now ascertainable, the same are to be disclosed to this Court when ascertained and are to be subject to the approval of this Court as fair and reasonable, and except with such approval no amounts or considerations covered by this Paragraph 50 shall be paid.

51. The Big Four is, as stated in the Plan, the owner of 50,001 shares of the capital stock of Petitioner, which is more than 50% of the total stock outstanding. The Plan as drafted stated that Petitioner contemplates that the identity and power and manner of selection of persons who are to be its directors and officers upon the confirmation of the Plan will be unchanged. The Plan is modified as provided in the Conclusions herein so that the Income Bondholders shall have one Director upon the Board of Directors of the Peoria and Eastern.

52. With respect to the continuation of the voting rights in Petitioner, control of Petitioner and the identity of and the power and manner of selection of and the persons who are to be directors and officers of Petitioner (no voting Trustees are proposed) upon the consummation of the Plan and their respective successors, the Plan makes full disclosure and as modified pursuant to the Conclusions herein, so that the Income Bondholders will have one member on the Board of Directors of the Peoria and Eastern, the Plan is adequate and equitable, in the best interests of creditors and stockholders of each class and consistent with public policy.

53. The extension of the Operating Agreement and the assumption of obligation and liability thereunder by the Big Four and the New York Central in respect of the First Consolidated Bonds has been duly authorized by the Commission.

Conclusions.

The Court hereby makes the following conclusions:

1. The Plan of Adjustment, modified so as to provide that the Income Bondholders shall, so long as any of the Income Bonds remain unpaid, have one Director upon the Board of Petitioner, is fair and equitable as an adjustment, affords due recognition to the rights of each class of creditors and stockholders and fair consideration to each class thereof adversely affected, and will conform to the law of the land regarding the participation of the various classes of creditors and stockholders.

2. Said modification does not substantially alter the basis for the specific findings included in the order made by the Interstate Commerce Commission under Section 20a of the Interstate Commerce Act and, accordingly, does not require that said Plan as so modified shall be resubmitted to the Interstate Commerce Commission; nor does said modification substantially or adversely affect the interests of any class or classes of creditors and, accordingly, does not require that said plan as so modified shall be resubmitted to any class of said creditors.

3. All corporate action required to authorize the issuance or modification of securities pursuant to the Plan has been duly taken.

4. The Plan and the adjustment provided thereby, modified as hereinbefore set forth, should be approved and confirmed.

Dated, July 23, 1940.

LEARNED HAND,
U. S. Circuit Judge.

WOOLSEY,
U. S. District Judge.

HULBERT,
U. S. District Judge.

DECREE OF DISTRICT COURT—Dated July 23, 1940 (R. 7)

IN THE

DISTRICT COURT OF THE UNITED STATES

FOR THE SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

DECREE

This cause coming on to be heard upon the Petition, the testimony of witnesses, documentary and other exhibits and the arguments and briefs of counsel and this Court, having considered the same and having made its findings and conclusions, hereby ORDERS, ADJUDGES and DECREES as follows:

ARTICLE I

PRIOR PROCEEDINGS HEREIN

Section 1. In this Decree the following terms have the following meanings respectively:

Petitioner or Peoria and Eastern.—The Peoria and Eastern Railway Company;

Big Four.—The Cleveland, Cincinnati, Chicago and St. Louis Railway Company;

New York Central.—The New York Central Railroad Company;

First Consolidated Bonds.—The First Consolidated Mortgage 4% Bonds of the Peoria and Eastern dated February 22, 1890, matured April 1, 1940;

First Consolidated Mortgage.—The First Consolidated Mortgage of the Peoria and Eastern, dated February 22, 1890, to the Central Trust Company of New York and Charles W. Fairbanks, as Trustee, under which mortgage the Central Hanover Bank and Trust Company is now the sole Trustee;

Income Bonds.—The Income Mortgage Bonds of the Peoria and Eastern, dated February 22, 1890, maturing April 1, 1990, in an aggregate principal amount not in excess of $4,000,000;

Income Mortgage.—The Income Mortgage of the Peoria and Eastern, dated February 22, 1890, and the supplement thereto dated March 25, 1890, made by the Peoria and Eastern to Central Trust Company of New York and Charles W. Fairbanks, Trustees, under which mortgage the Central Hanover Bank and Trust Company is now the sole Trustee;

Operating Agreement.—The agreement dated February 22, 1890 and the supplement thereto of the same date between the Big Four and the Peoria and Eastern, pursuant to which the property of the Peoria and Eastern has been operated since 1890;

Purchase Money Lien.—The Lien of $5,000,000 reserved in the deed made by Charles H. Coster and Samuel Spencer to the Big Four, dated February 22, 1890, of the portion of the former Ohio, Indiana and Western Railway extending from the City of Indianapolis, Indiana, to the City of Springfield, Ohio, herein called the Springfield Division;

Commission.—The Interstate Commerce Commission;

Plan.—The Plan of Adjustment under Chapter XV of the Bankruptcy Act, dated January 10, 1940, of The Peoria and Eastern Railway Company, in respect of the extension of the date of maturity from April 1, 1940 to April 1, 1960 of a part of the principal of the Peoria and Eastern Railway Company's First Consolidated Mortgage Bonds dated February 22, 1890.

Section 2. The Petition in this proceeding was filed in the office of the Clerk of this Court on March 29, 1940. A copy of the Order of the Commission containing the findings required under clauses (a), (b) and (c) of paragraph (2) of the first sentence of Section 710 of the Bankruptcy Act and authorizing the modification and issuance of securities as provided in the Plan was filed with the Petition and made a part thereof.

Section 3. Immediately following the filing of the Petition there was convened a Special Court of three Judges, pursuant to Section 713 of the Bankruptcy Act, in the manner provided by Section 266, as amended, of the Judicial Code. Such Judges, namely, Learned Hand, U. S. Circuit Judge, John M. Woolsey, U. S. District Judge, and Murray Hulbert, U. S. District Judge, met and a hearing was held by this Court on the 29th day of March, 1940. After such hearing, this Court being satisfied that the Petition complied with Chapter XV of the Bankruptcy Act and had been filed in good faith, entered its order dated March 29, 1940 approving the Petition as properly filed under said Chapter XV and fixing April 29, 1940, at 3:00 o'clock in the afternoon at the Court House of the District Court of the United

States for the Southern District of New York for a hearing to be held promptly after the filing of the Petition and directing the form of and the giving of notice of such hearing and reserving jurisdiction, all as more fully provided in said Order.

Section 4. The Petitioner duly gave notice of said hearing on April 29, 1940, by mailing on or before April 5, 1940, a copy of the notice in the form required by said Order, to the Central Hanover Bank and Trust Company, as Trustee, under the Indenture securing the First Consolidated Bonds of Petitioner, to the Secretary of the Treasury, and to each known holder of the securities of Petitioner, whether or not such security holder was affected by the Plan, at their respective addresses as shown by the records of Petitioner, to the extent that Petitioner had record of such addresses, and by publication thereof at least once a week (on a business day of each week) for two successive weeks in the New York Times, a newspaper published and of general circulation in the Borough of Manhattan, City of New York, and in the Chicago Tribune, a newspaper published and of general circulation in the City of Chicago, Illinois, the first such publication being on April 5, 1940.

Section 5. Pursuant to said Order and said notice, this cause came on for a public hearing before this Court (all said Judges being present) at a public session thereof in the United States Court House in the Borough of Manhattan, City and State of New York, on April 29, 1940, on May 8, 1940, May 21, 1940 and June 11, 1940. Petitioner appeared by counsel and introduced evidence both oral and documentary. Interventions were requested by and allowed to William Carnegie Ewen, Lewis L. Clark and Maurice

D. Adams, acting as a committee representing the holders of $300,000 in principal amount of the Income Bonds, and Donald N. Gilbert, Harold C. Yeager and George A. Carey, representing the holders of more than $300,000 in principal amount of the First Consolidated Bonds. Both committees appeared by counsel at said hearings and introduced evidence, both oral and documentary, and objections to the Plan were made on the part of both committees of intervenors. All persons requesting intervention were allowed to intervene. No persons other than the above committees asked to appear or appeared in this proceeding.

Section 6. On July 8, 1940, an opinion of this Court (concurred in by all of the said Judges) was filed setting forth the conclusions of this Court, with the reasons therefor, and holding, (1) that the Plan should be modified so as to provide that the Income Bondholders shall, so long as any of the Income Bonds remain unpaid, have one director upon the Board of Directors of Petitioner; and holding, (2) that with such modification the Plan complies with and satisfies the requirements of Chapter XV of the Bankruptcy Act and should be approved and confirmed; and holding, (3) that such modification of the Plan does not substantially alter the basis for the specific findings included in the Report and Order of the Commission under Section 20 (a) of the Interstate Commerce Act and accordingly does not require that said Plan as so modified shall be resubmitted to the Commission; and holding, (4) that such modification of the Plan does not substantially or adversely affect the interests of any class or classes of creditors and, accordingly, does not require that such Plan as so modified shall be resubmitted to any class of said creditors. The Plan as modified as aforesaid is hereinafter called the Plan as Modified.

ARTICLE II

Confirmation of the Plan as Modified

Section 7. The Plan as Modified and the adjustment provided thereby are hereby approved and confirmed. The provisions of the Plan as Modified and the instruments executed pursuant to the Plan as Modified for the purpose of carrying the same into effect shall be final and binding on (1) Petitioner; (2) each and all creditors and security holders of Petitioner, including the holders of certificates of deposit of Petitioner; (3) all Trustees under any indentures or other agreements securing any claims against Petitioner or its property; and (4) all other persons whatsoever. The rights of all creditors and security holders with respect to claims and securities affected by the Plan as Modified shall be only those provided by the Plan as Modified as evidenced and specified in the instruments executed pursuant thereto. Petitioner shall have full power and authority and shall put into effect and carry out the Plan as Modified and the orders of this Court relative thereto and issue the securities provided by the Plan as Modified and execute the instruments provided by the plan as Modified to be executed, all as hereinafter provided without further reference to or authority from the Commission or any other authority, State or Federal.

Section 8. All persons referred to in Section 7 hereof are hereby perpetually restrained and enjoined from taking or continuing any action whether by the making or claiming of any payment or by the institution or prosecution of any judicial proceeding or otherwise in any way without

limitation that would be inconsistent with the provisions of the Plan as Modified, as evidenced and specified in the instruments executed pursuant thereto, or of this Decree.

Section 9. All interest on the Preferred Bonds of The Indiana, Bloomington and Western Railway Company, which bonds are to be paid as provided in the Plan as Modified, accruing subsequent to April 1, 1940, and prior to the date fixed for the payment of such bonds, shall be paid by Petitioner at the time of the payment of such bonds. All interest on the portion of the principal of the First Consolidated Bonds, which is to be paid as provided in the Plan as Modified, accruing subsequent to April 1, 1940, and prior to the date fixed for such partial payment, shall be paid by Petitioner at the time of such partial payment.

Section 10. The sum of $5,000,000 to be paid by the Big Four in satisfaction of the Purchase Money Lien shall, as soon as practicable following the expiration of sixty days from the date of the entry of this Decree, be applied by the Central Hanover Bank and Trust Company as Trustee of the First Consolidated Mortgage (as provided for in Section 2 of Article III of the Plan and in Article I of the proposed Supplemental Indenture dated as of April 1, 1940, and attached to the Petition herein as Exhibit B), as follows:

(a) The sum of $846,000 to the payment of the principal of the outstanding Preferred Bonds of The Indiana, Bloomington and Western Railway Company, originally in the aggregate principal amount of $1,000,000, of which $846,000, principal amount are now outstanding, and following such payment the mortgage of The Indiana, Bloomington and

Western Railway Company securing such bonds shall be satisfied and discharged of record; the $846,000 principal amount of such bonds now outstanding, the principal amount of such bonds now held in the treasury of the Peoria and Eastern and the $124,000, principal amount of First Consolidated Bonds of the Peoria and Eastern now held in the Sinking Fund for such bonds shall be cancelled; the moneys necessary to pay the interest accrued upon such Bonds from the last interest payment date to the date fixed for the payment thereof shall be furnished by the Peoria and Eastern to the Trustee upon request of the Trustee;

(b) The sum of $384,500 on account of the First Consolidated Bonds of the Peoria and Eastern pledged by the Peoria and Eastern as part collateral security for its promissory note in the amount of $500,000 held by the Securities Corporation of the New York Central Railroad and secured by First Consolidated Bonds in the amount of $500,000 and 1730 shares of the stock of the Peoria and Pekin Union Railway Company, and the moneys so paid shall be applied in reduction of the principal of said note; and upon such payment $290,000, principal amount of such bonds shall be released from such pledge and cancelled and the principal of the $210,000, principal amount of the remaining bonds so pledged shall be reduced to $115,500 by the application of $94,500 (of said sum of $384,500) on account of the principal thereof (on the basis of $450. for each $1,000 bond), and the holder of said note shall (as provided in the Plan as Modified) thereupon accept said cash and said $115,500 of reduced principal amount of First Consolidated Bonds in satisfaction of said note; the 1730 shares of stock of the Peoria and Pekin Union Railway Company shall, upon their release from pledge as security for said note, be

pledged with the Trustee under the First Consolidated Mortgage as additional security, as provided for in the Supplemental Indenture attached to the Petition herein as Exhibit B; the interest accrued on said note from the last interest payment date to the date of the payment of the note shall be paid by the Peoria and Eastern;

(c) The sum of $3,769,200 ratably on account of the principal of the remaining $8,376,000, principal amount of First Consolidated Bonds (being at the rate of $450 for each $1,000 bond), reducing the amount unpaid on account of the principal amount of such remaining bonds to $4,606,800;

(d) The sum of $300 remaining of said $5,000,000 to be paid in satisfaction of the Purchase Money Lien after the payments provided for in subdivisions (a), (b) and (c) above, shall be paid to the Trustee under the First Consolidated Mortgage and applied by such Trustee in the purchase in the market at the lowest price obtainable, not in excess of the principal amount and accrued interest (which interest shall be paid by the Peoria and Eastern to the Trustee upon request therefor) of First Consolidated Bonds which shall have been reduced in principal amount and the maturity date extended as provided for in the Plan as Modified (or bonds issuable in exchange therefor as provided in the Supplemental Indenture attached to the Petition herein as Exhibit B); the bonds so purchased by the Trustee shall, following such purchase, be cancelled.

In case, however, of the payment by the Big Four of said sum of $5,000,000 in satisfaction of the Purchase Money Lien to the Central Hanover Bank and Trust Company as Trustee prior to the expiration of sixty days from the date of the entry of this Decree, Petitioner shall im-

mediately following such payment (1) mail to each known holder of the First Consolidated Bonds a notice to the effect that such payment has been made and that the First Consolidated Bonds, or the Certificates of Deposit therefor issued pursuant to the Plan as Modified, are required by this Decree (and they are hereby so required) to be forthwith presented to the Central Hanover Bank and Trust Company as Trustee under the First Consolidated Mortgage at its office or agency at 70 Broadway in the Borough of Manhattan, City and State of New York, for payment of $450 on account of the principal of each $1,000 Bond (other than the Bonds mentioned in sub-divisions (a) and (b) above of this Section) and that interest shall cease as to the portion of the principal so paid from the date of payment thereof or at the expiration of fifteen days from the date of such notice, whichever date shall be the earlier; and (2) shall, commencing with the date of the mailing of said notice, publish a notice substantially to the above effect twice a week for two successive weeks in New York Times, a newspaper published and of general circulation in the City of New York, State of New York, and in Chicago Tribune, a newspaper published and of general circulation in the City of Chicago, State of Illinois. Upon the presentation of the First Consolidated Bonds pursuant to such notice, the Central Hanover Bank and Trust Company as Trustee shall pay from the said sum of $5,000,000 paid by the Big Four in satisfaction of the Purchase Money Lien, the sum of $450 on account of the principal of each $1,000 of First Consolidated Bonds (other than the Bonds mentioned in subdivisions (a) and (b) of this Section) and shall note such payment upon the Certificates of Deposit, where Certificates of Deposit shall have been issued in respect of the First Consolidated Bonds, and, upon the

First Consolidated Bonds, where no Certificate of Deposit shall have been issued in respect thereof. Interest shall cease as to $450 of the principal of each $1,000 of First Consolidated Bonds mentioned in subdivision (c) of this Section at the date of such principal payment or at the expiration of fifteen days from the date of the above notice, whichever date shall be the earlier. This Paragraph, if a modification of the Plan, does not substantially alter the basis for the specific findings included in the order made by the Commission under Section 20(a) of the Interstate Commerce Act authorizing the issuance or modification of securities as provided in the Plan, and does not substantially or adversely affect the interest of any class or classes of creditors and this Court hereby so determines and hereby approves and confirms the same.

Section 11. The date of maturity of the portion unpaid of the principal of the First Consolidated Bonds (after the payment on account of the principal thereof provided for in Section 10 above) aggregating $4,722,300, shall, as soon as practicable following the expiration of sixty days from the date of the entry of this Decree, be extended without impairment of the lien of the Indenture of Mortgage securing such bonds (but with the Purchase Money Lien discharged by payment as provided in Section 10 above), from April 1, 1940 to April 1, 1960, such extended Bonds (and the Bonds exchangeable therefor under the provisions of the Supplemental Indenture dated as of April 1, 1940, attached to the Petition herein as Exhibit B) to continue to bear interest during the period of their extension at the present rate of 4% per annum, payable semi-annually on April 1 and October 1.

Section 12. The Peoria and Eastern and the Central Hanover Bank and Trust Company as Trustee under the First Consolidated Mortgage are hereby authorized, as soon as practicable following the expiration of sixty days from the date of the entry of this Decree, to execute and carry into effect a Supplemental Indenture in substantially the form of the proposed Supplemental Indenture dated as of April 1, 1940, which is attached to the Petition herein as Exhibit B, the form and terms of which Supplemental Indenture and of the Exchangeable Bonds, extension agreement, notations, legends and new coupons set forth therein are hereby respectively approved. Such Supplemental Indenture, Exchangeable Bonds, extension agreement, notations, legends and new coupons are consistent with the Plan as Modified and this Decree and are necessary or desirable for the due and proper effectuation of the Plan as Modified and this Decree.

Section 13. The rights of the holders of the First Consolidated Bonds shall, following the execution of the Supplemental Indenture referred to in Section 12 hereof, be only those provided in the First Consolidated Mortgage, as supplemented and modified by such Supplemental Indenture, whether or not such holders shall have assented to the Plan or this Decree or said Supplemental Indenture or the extension agreement, and whether or not such extension agreement shall have been annexed to the First Consolidated Bonds. The First Consolidated Mortgage as so supplemented and modified by the Supplemental Indenture referred to in Section 12 hereof shall be binding upon all such holders, upon the Peoria and Eastern and upon the Central Hanover Bank and Trust Company as Trustee thereunder and upon any other trustee or trustees

which may at any time succeed to the trusts now vested in the Central Hanover Bank and Trust Company thereunder.

Section 14. As soon as practicable after the execution of the Supplemental Indenture dated as of April 1, 1940, referred to in Section 12 above, Petitioner shall (1) mail to each known holder of the First Consolidated Bonds a notice to the effect that the First Consolidated Bonds are required by this Decree (and they are hereby so required) to be presented forthwith to the Central Hanover Bank and Trust Company at its office or agency in the Borough of Manhattan, City and State of New York (such notice to designate the address of such office or agency and to be accompanied by an appropriate form of transmittal letter) for the payment on account of the principal thereof provided for in the Plan as Modified, if such payment has not already been made, for the attachment thereto of the extension agreement and coupons, and for the stamping or imprinting thereon of the notations or legends provided for in the Supplemental Indenture hereinabove in said Section 12 authorized; and (2) publish a notice substantially to the above effect twice a week for two successive weeks in New York Times, a newspaper published and of general circulation in the City of New York, State of New York, and in Chicago Tribune, a newspaper published and of general circulation in the City of Chicago, State of Illinois.

Upon presentation from time to time of such securities at the office or agency of the Central Hanover Bank and Trust Company as aforesaid, and payment on account of the principal thereof provided for in the Plan as Modified

and in Section 10 hereof having been made, Petitioner shall annex or cause to be annexed to each of the First Consolidated Bonds the extension agreement and coupons and shall stamp or imprint, or cause to be stamped or imprinted thereon the notations and legends provided for in the said Supplemental Indenture, all as hereinabove authorized, and such securities shall thereupon be returned to or on the order of the persons so presenting the same, or upon request of the persons presenting the same, Exchangeable Bonds shall, as hereinafter provided, be issued in exchange therefor. On request at the time of presentation, the security holders so presenting such securities shall be reimbursed by the Peoria and Eastern for all ordinary expenses of forwarding their securities for presentation, including the cost of registration and insurance. In case the holders of the First Consolidated Bonds at the time of presentation of the same for extension and stamping shall request the issue to them, in exchange for the bonds so presented, of the Exchangeable Bonds provided for in Article IV of the said Supplemental Indenture, then Exchangeable Bonds as provided for in Article IV of the Supplemental Indenture shall be issued in respect of the reduced aggregate principal amount of the First Consolidated Bonds presented by the holders making such requests.

Section 15. Petitioner and the Central Hanover Bank and Trust Company as Trustee under the mortgage securing the First Consolidated Bonds are hereby authorized and directed, as soon as practicable following the expiration of sixty days from the date of entry of this

Decree, to take or cause to be taken all such other and further steps, including the pledge with the Trustee under the First Consolidated Mortgage of the 1730 shares of stock of the Peoria and Pekin Union Railway Company as provided for in the Supplemental Indenture referred to in Section 12 hereof, and perform or cause to be performed all such other and further acts, and do or cause to be done all such other and further things not inconsistent with the provisions of the Plan as Modified or this Decree as may be necessary or appropriate for the due, proper and full effectuation of the Plan as Modified and this Decree and the execution of the Supplemental Indenture provided for in Section 12 hereof.

Section 16. Upon the payment of the Purchase Money Lien by the Big Four, the Central Hanover Bank and Trust Company as Trustee under the First Consolidated Mortgage and as Trustee under the Income Mortgage, and the Peoria and Eastern, shall execute an instrument in proper form discharging the Purchase Money Lien in respect of the property affected thereby.

Section 17. All expenses of effectuating the Plan as Modified and this Decree and of executing the Supplemental Indenture shall be paid by the Peoria and Eastern, but no such payment shall be made by the Peoria and Eastern except as provided in Section 21 hereof, unless and until the same shall have been approved and authorized by the further order of this Court.

Section 18. Notwithstanding any other provisions of this Decree the form of the Supplemental Indenture dated as of April 1, 1940, hereinabove in Section 12 approved

and authorized may, prior to the execution thereof, be completed by filling in the blank spaces and adding acknowledgments and, if and where necessary, be corrected so as to eliminate any clerical error or to conform any provision to corresponding provisions elsewhere in the same Indenture; a list of all such corrections shall be incorporated in the report requested by Section 19.

Section 19. As soon as practicable after the execution and delivery of the Supplemental Indenture authorized in Section 12 hereof and the attachment of the extension agreement to and the stamping and imprinting of the said notation upon the First Consolidated Bonds, Petitioner shall file herein its report describing in reasonable detail the action taken pursuant to this Decree.

ARTICLE III

Miscellaneous

Section 20. This Court hereby reserves full jurisdiction to correct or perfect this Decree, to take any other or further action in aid of this Decree, to consider and act upon all matters dealt with in any report made relating to the effectuation of the Plan as Modified and this Decree and otherwise to take all such supplementary action as this Court may deem proper in the premises; provided, however, that no action taken pursuant to this Section shall impose, or result in, any liability on anyone for or in respect of any action theretofore taken in accordance with this Decree or any instrument executed pursuant thereto.

Section 21. The Court hereby approves the following expenses and authorizes the payment thereof:

Printing and postage	$ 2,200.00
Advertising	1,800.00
Cost of Certificates of Deposit.....	200.00
Trustee's charges in connection with deposit of bonds, issuance of Certificates of Deposit, stamping of Bonds, re-issue of Bonds, etc.....	12,800.00
Cost of engraving new Bonds.....	7,000.00
Trustee's fees for authenticating new Bonds	2,500.00
Total.....	$26,500.00

The Court hereby reserves full jurisdiction to consider and approve and authorize or disapprove, after hearing, upon due notice, expenses of every kind not herein approved or authorized.

Section 22. The Peoria and Eastern shall pay in full in cash upon notice and demand any and all Federal taxes finally determined to be due from it without requiring proof thereof in this proceeding and without prejudice by reason of not having been proved herein.

Section 23. As soon as certified copies of this Decree shall be prepared and made available by the Clerk of this Court, the Peoria and Eastern shall send by registered mail, postage prepaid, one copy thereof each to the Commission, the Securities and Exchange Commission, the Secretary of the Treasury, the New York Stock Exchange, and the Central Hanover Bank and Trust Company as Trustee under the mortgage securing the First Consoli-

dated Bonds. As soon as practicable after the entry of this Decree, the Peoria and Eastern shall cause notice that the Plan has been approved and confirmed to be published twice a week for two successive weeks in New York Times, a newspaper published and of general circulation in the City of New York, State of New York, and in Chicago Tribune, a newspaper published and of general circulation in the City of Chicago, State of Illinois.

Section 24. All questions concerning the amount and validity of the accounts between the Big Four, the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the Big Four seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or Big Four must prove and establish their right to do so.

Section 25. The Petitioner shall by appropriate action incorporate provisions in its charter and by-laws, to authorize and regulate the election of one director by the Income Bondholders.

Dated, July 23, 1940.

LEARNED HAND,
United States Circuit Judge.

WOOLSEY,
United States District Judge.

HULBERT,
United States District Judge.

ORDER SUPPLEMENTAL TO DECREE—Dated April 9, 1941, of District Court (R. 10)

IN THE

DISTRICT COURT OF THE UNITED STATES

FOR THE SOUTHERN DISTRICT OF NEW YORK

[SAME TITLE AS FINAL DECREE]

ORDER SUPPLEMENTAL TO DECREE

Upon due consideration of the Petition of The Peoria and Eastern Railway Company, herein called the Petitioner, verified and filed herein on January 8th, 1941 under Chapter XV of the Bankruptcy Act, as amended, praying for an order that the report of Petitioner as contained in said Petition be approved; that the Court approve as fair and reasonable payment by Petitioner of certain additional expenses and fees, as recited in said Petition, in connection with said Plan of Adjustment; that the Court approve the execution of the proposed agreement submitted with said Petition as a compliance with the provisions of Section 25 of the Decree entered herein on July 29th, 1940, relating to representation of the Income Mortgage Bondholders upon the Board of Directors of Petitioner; and that Section 24 of the said Decree be amended in certain particulars; and

Upon due consideration of the respective petitions for allowances filed herein of William Carnegie Ewen and others as a committee of the Income Mortgage Bondholders Intervenors dated and verified January 8, 1941, of Charles S. Aronstam as counsel for such Income Bondholders Com-

mittee, dated and verified December 21, 1940, and of Scribner and Miller and Alfred E. Smith, Jr. as counsel for a Committee of First Mortgage Bondholders Intervenors dated and verified January 13, 1941; and

After consideration of the arguments and briefs of counsel and the Court being fully advised in the premises and having filed its opinion herein, dated April 3, 1941, it is Ordered:

1. The report of Petitioner contained in the Petition filed herein dated January 8th, 1941 is hereby approved and ordered filed.

2. The Court approves as fair and reasonable payment by Petitioner of the following fees and expenses in connection with the said Plan of Adjustment, in addition to those approved in Section 21 of the Decree:

Expenses on account of imprinting legends on Bonds	$ 500.00
Expenses for advertising various notices	1,760.45
Expenses for printing, postage, insurance, registration, etc.	2,683.76
Fee for listing extended Bonds on New York Stock Exchange	600.00
Expense of transcript of stenographer's minutes	390.40
Recording fee (Supplemental Indenture, satisfaction pieces) estimated	250.00
Total —	$6,184.61

and the fees of Messrs. Larkin, Rathbone & Perry for services as Counsel to the Central Hanover Bank and Trust Company, as Trustee, in the sum of $2,000.00.

3. The Court approves the execution of the proposed agreement, a copy of which is hereto attached as Exhibit "A" (Paragraph Second of Exhibit "C" attached to the Petition of Petitioner herein dated January 8, 1941, having been modified in accordance with the opinion of the Court herein dated April 3, 1941), among Petitioner, the Big Four, The New York Central Railroad Company and the Central Hanover Bank and Trust Company, as Trustee of the Petitioner's Income Mortgage, as a compliance with the provisions of Section 25 of the Decree.

4. The Court hereby amends Section 24 of the Decree so that such Section as modified will read as follows:

> "Section 24. All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and reserved for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', *upon objection by the representative of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so.*"

Order Supplemental to Decree—April 9, 1941

5. The petitions of the Intervenors and their counsel herein for allowances are hereby dismissed, without costs, on the ground that the Court is without jurisdiction to grant such allowances.

Dated, April 9, 1941.

L. HAND
United States Circuit Judge.

WOOLSEY
United States District Judge.

HULBERT
United States District Judge.

[Exhibit A, dealing with the election of the Income Bondholder director, omitted.]

AGREEMENT—Dated October 30, 1889, Between Reorganization Committee of The Ohio, Indiana and Western Railway Company and The Cleveland, Cincinnati, Chicago and St. Louis Railway Company (R. 23; Ex. 3)

AGREEMENT made this 30th day of October, 1889, by and between THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY (hereinafter called the Cleveland Co.) and C. H. COSTER, SAMUEL SPENCER, GEORGE T. BLISS and ANTHONY J. THOMAS, the Committee for reorganization of the Ohio, Indiana and Western Railway Company (hereinafter called the Committee).

WHEREAS, The Committee is about to attempt the reorganization of the Ohio, Indiana and Western Railway Company substantially upon the basis set forth in the plan and agreement of reorganization hereunto annexed and made part of this contract;

AND WHEREAS, It is in contemplation to separate the lines of railway of said Company into the Western line, comprising the part from Indianapolis westward, and the Eastern line, comprising the part from Indianapolis eastward, substantially as the said lines formerly existed:

NOW, THEREFORE, THESE PRESENTS WITNESS, that the said Cleveland Co. covenants and agrees that, when the Committee shall have so far carried out the said reorganization as that the said Western line and the said Eastern line shall have become or can be separated, then, upon transfer and delivery to it of one-half of the stock of the Company owning said Western line issued under said reorganization, it will purchase or otherwise take over the said Eastern line subject to and charged with a purchase money lien, on

the property only, amounting to $5,000,000 payable in one hundred years, with interest thereon in the meantime at 4 per cent. per annum, payable annually out of income alone and non-cumulative. The said Western and Eastern lines being now subject to the lien of prior bonds for $500,000, it is understood that said prior bonds or bonds having an equal lien issued in place thereof as provided in the reorganization agreement shall have the benefit of said purchase money lien. The said purchase money lien shall be transferred by the Committee to the Company owning said Western line (and hereinafter called the Western Company) as security for the principal and interest of the new bonds to be issued under said plan of reorganization, the interest on said purchase money lien to be applied in payment of the interest on the said prior bonds and the new First Consolidated Mortgage Bonds to be issued under said plan. The Cleveland Co. will also simultaneously enter into a lease or other operating contract, whereby it shall undertake the operation and management of said Western line, and agree (1) that the net earnings of said Western line shall be applied likewise to the payment of the interest to accrue on the said prior bonds, also on $1,000,000 other prior bonds having a lien on the Western line only, and on said new First Consolidated Mortgage Bonds, and (2) that the balance of such net earnings from the Western line and income derived from the lien on the Eastern line, shall, after payment of said interest, be paid over to the Western Company. Said lease or contract shall also contain covenants that the Cleveland Co. shall provide for the due and punctual payment, as it accrues, of the interest on the said $1,500,000 prior bonds and on all said new First Consolidated Mortgage Bonds which may at any time be outstanding, and shall guarantee that the net earnings and income

of the Western Company derived from both said lines shall not be less than $412,200 a year, to be increased by the sum of $40 a year for each and every of said First Consolidated Mortgage Bonds issued in excess of $9,430,000 of said bonds, as provided in said plan of reorganization, and that the Cleveland Co. shall look only to future surplus net earnings and income of the Western Company derived from both said lines for its reimbursement of any sums advanced to make good any deficiency in said net earnings and income, with interest at six per cent. per annum.

The said lease or contract of the Western line shall be for a term of years at the election of the Cleveland Co., but not less than 50 years, and shall be assignable in whole or in part as additional security for the said First Consolidated Mortgage Bonds, and shall also contain covenants whereby said Cleveland Co. shall undertake to maintain said Western line and the rolling stock necessary for the operation of said Western line, and pay all taxes thereon, or upon the earnings or income of said Western line, as well as rentals or other like charges, and to indemnify and save harmless said Western Company from all claims arising out of the operation or management thereof, and also such other covenants, terms and conditions as may be reasonably required by said Committee pursuant to the plan of reorganization or for the more perfect protection of the holders of said prior bonds and said new First Consolidated Mortgage Bonds, and the new income bonds and stock to be issued under said plan of reorganization, and the rights and interests intended to be granted to them.

IT IS FURTHER COVENANTED AND AGREED, that in the event that, by reason of any legal impediment, this agreement

cannot be carried out in its exact terms, a substantial compliance therewith may be required by either party from the other.

In witness whereof, the party of the first part has hereunto set its corporate seal and caused these presents to be signed by its president thereunto duly authorized, and the parties of the second part have hereunto set their hands and seals, the day and year first above written.

C. H. Coster,
Samuel Spencer,
George T. Bliss,
Anthony J. Thomas,
Committee.

Attest
E. F. Osborn,
Secretary.

The Cleveland, Cincinnati, Chicago and
St. Louis Railway Company

by M. E. Ingalls,
President.

[Reorganization Agreement Omitted]

OPERATING AGREEMENT—Dated February 22, 1890, Between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company and The Peoria and Eastern Railway Company (R. 23; Ex. 11)

THIS INDENTURE, made this twenty-second day of February, one thousand eight hundred and ninety, by and between the CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY, party of the first part (hereinafter called the Cleveland Co.), and the PEORIA AND EASTERN RAILWAY COMPANY, party of the second part (hereinafter called the Peoria Co.), WITNESSETH:

WHEREAS the Peoria Co. has acquired a line of railroad extending westward from the boundary line between the States of Illinois and Indiana to Pekin, in the State of Illinois, together with rights and interests in the tracks and other property of the Peoria and Pekin Union Railway Company, hereinafter called the "Illinois part" of said line of railroad, and has also acquired a leasehold interest in a line of railroad extending from the boundary line between the States of Illinois and Indiana to the tracks of the Indianapolis Union Railway Company in or near Indianapolis, in the State of Indiana, with the right to use the tracks and certain other property of the Indianapolis Union Railway Company, hereinafter called the "Indiana part" of said line of railroad, and which said lines of railroad were formerly the property of the Ohio, Indiana and Western Railway Company, and which said "Illinois part" and "Indiana part" are subject to the lien of a certain mortgage to secure bonds known as Preferred Bonds of the Indiana, Bloomington and Western Railway Company for one million dollars, executed by said last named company on or about the 15th day of April, 1879, to the Central Trust Company of New

York as trustee, and also subject to the lien upon said "Illinois part" and said "Indiana part," as well as upon the line of railroad extending from Indianapolis, Indiana, to Springfield, in the State of Ohio, formerly belonging to the said Ohio, Indiana and Western Railway Company, for five hundred thousand dollars of preferred bonds secured by a mortgage executed by the Ohio, Indiana and Western Railway Company to the Central Trust Company of New York, as trustee, bearing date the second day of April, one thousand eight hundred and eighty-eight; and

WHEREAS the Peoria Co. has issued a certain series of its First Consolidated Mortgage Bonds, dated February 22d, 1890, for an aggregate amount of $10,000,000, payable on the first day of April, 1940, at its office or agency in the City of New York, with interest thereon from the first day of April, 1890, at the rate of four per cent. per annum, payable semi-annually at said office or agency in accordance with coupons for such interest annexed to said bonds, and has secured the payment of said bonds by a first mortgage of all its corporate property and franchises to the Central Trust Company of New York and Charles W. Fairbanks of Indianapolis as trustees, and which said first mortgage and said prior mortgages are superior to these presents; and is about to issue a certain series of its Income Mortgage Bonds dated February 22d, 1890, for an aggregate amount of $4,000,000, payable in 100 years, and bearing interest at not exceeding four per cent. per annum, and non-cumulative, payable when and only if, and to such extent, as earned, beginning April 1, 1891, and annually thereafter, out of the net earnings of the property, and is about to secure the payment of said last mentioned bonds by a second mortgage of all its corporate property and franchises, to said Central

Trust Company of New York and Charles W. Fairbanks as trustees, and which said second mortgage shall be subject to these presents;

AND WHEREAS the railways of the parties hereto connect at Indianapolis, and it will be beneficial to the business and traffic of said railways that the same be put under one management:

NOW, THEREFORE, THESE PRESENTS WITNESS, that the Cleveland Co., in consideration of the premises, and of one dollar to it in hand paid by the Peoria Co., the receipt whereof is hereby acknowledged, hereby contracts and arranges with the Peoria Co. for running the railroad of the Peoria Co. as follows:

FIRST.—The Peoria Co. hereby grants unto the Cleveland Co., its successors and assigns, subject to said first consolidated mortgage and to said prior mortgages, the right to use and operate that portion of its railroad known as the "Illinois part," and the Cleveland Co. agrees that it shall and will from henceforth and during the term herein limited, use, maintain and operate said "Illinois part" upon the terms and conditions herein prescribed; and the Peoria Co. hereby also assigns and transfers, subject to said first consolidated mortgage and said prior mortgages, for the period during which these presents shall continue, its leasehold interest in said "Indiana part," and all the rolling stock and equipment of the Peoria Co. and which said rolling stock and equipment shall be considered as included in said "Indiana part" whenever said "Indiana part" is herein mentioned or referred to; and the Cleveland Co. shall and will henceforth and during the period of fifty years from

April 1st, 1890, and for such further time thereafter as it may elect, use and operate said "Indiana part" and said "Illinois part" as railways in such manner as to satisfy the requirements of law in the States and jurisdictions in which the same are or shall at any time be situated, itself providing and furnishing, at its own cost and expense, all other rolling stock and equipment, labor and supplies necessary for that purpose; and also at all times during its said use and operation thereof, also at its own cost and expense, shall and will keep up and maintain all said "Indiana part" and said "Illinois part" of said line of railroad and all said rolling stock and equipment in good working order, and restore and renew all parts thereof as may be necessary to that end; and also shall and will pay all taxes on said "Indiana part" and said "Illinois part" of said line of railroad or upon the earnings or income thereof, as well as rentals reserved, or other like charges, payable for such use in respect of any part or parts thereof: and also shall and will indemnify and save harmless the Peoria Co. from any and all claims arising out of the operation or management thereof; and also at its own cost and expense shall and will do, perform and comply with all and singular the covenants, terms and conditions accepted or undertaken by the Peoria Co. in the conveyances, deeds and leases to it of the same or of any parts thereof, or in said mortgages so given by it to secure said bonds, excepting always the payment of the principal of said bonds, or of said prior bonds, it being understood and agreed that the Cleveland Co. does not assume the payment of such principal or any part of it.

SECOND.—The Cleveland Co. hereby covenants and agrees to and with the Peoria Co., its successors and assigns, and to and with all and singular the persons and

parties who may at any time be or become the holders of the bonds secured by said first consolidated mortgage hereinbefore mentioned, or of any of them, that it shall and will provide for and make good any deficiency which may at any time occur in the fund necessary for the due and punctual payment as it accrues of the interest on the two series of bonds secured by the said prior mortgages hereinbefore mentioned and of the interest on all of the said First Consolidated Mortgage Bonds of the Peoria Co. which may at any time be outstanding, and of any tax or taxes which the Peoria Co. may be required to pay or retain from said interest on any of said bonds (it being understood and agreed that said interest is to be paid without deduction for any such tax or taxes), after devoting to such payment of interest the net income which may arise from the purchase money lien of five millions of dollars on that part of the railroad formerly of the Ohio, Indiana and Western Railway Company between Indianapolis, Indiana, and Springfield, Ohio, and the net earnings derived from said "Indiana part" of said line of railroad and the net earnings derived from said "Illinois part" of said line of railroad; and the Cleveland Co. guarantees that the net earnings and income from said three sources, so actually applied to the payment of said interest, shall not be less than four hundred and twelve thousand two hundred dollars in each and every year of the fifty years for which it by these presents undertakes the use and occupation of said "Indiana part" of said line of railroad; and it further agrees that such guaranty shall be increased by the sum of forty dollars in each and every year for each and every one thousand dollars of said First Consolidated Mortgage Bonds issued in excess of nine million four hundred and thirty thousand dollars; and that the Peoria Co. may transfer and assign the covenants con-

tained in this second clause of these presents and all benefits thereof to the trustees of said mortgage executed by it as aforesaid to secure its said First Consolidated Mortgage Bonds, and that upon such transfer and assignment, said covenants shall be deemed and taken to be a direct and absolute obligation and guaranty of the Cleveland Co. to the said trustees and to all and singular the persons and parties, who may at any time be or become the holders of said First Consolidated Mortgage Bonds or of any of them, for the payment of all the interest to accrue thereon and on the bonds secured by said prior mortgages, as and when it shall become payable, and that the Cleveland Co. shall, if thereunto requested by the trustees of said First Consolidated Mortgage, execute and deliver to them and by way of further assurance, a separate and independent covenant and agreement to the effect hereinabove provided.

THIRD.—The Cleveland Co. is to receive all earnings and income of the use and operation of said "Indiana part" and of said "Illinois part" of said line of railroad, and of said rolling stock and equipment, and apply the net earnings of each year arising from the same (to be ascertained by deducting from the earnings and income of the year from its use and operation of said "Illinois part" and said "Indiana part," the expenses of operation and maintenance during such year, including taxes, assessments, insurance, rental and other like charges, and the cost of repairs, renewals and reasonable betterments to the said "Illinois part" and the said "Indiana part," necessary for their economical and efficient operation), together with the net income from the purchase money lien of $5,000,000 on the part of the railroad formerly of the Ohio, Indiana and Western Railway Company between Indianapolis, Indiana, and

Springfield, Ohio, to the payment of the interest as and when it shall mature and become payable upon the said two series of bonds, secured by prior mortgages upon said line of railroad, to wit: $1,000,000 of bonds issued by the Indiana, Bloomington and Western Railway Company and $500,000 of Preferred Bonds issued by the Ohio, Indiana and Western Railway Company, and to the payment of the interest as and when it shall become payable upon said First Consolidated Mortgage Bonds of the Peoria Co. After reimbursing itself out of what shall remain of such net earnings and income of the year, not applied as aforesaid to the payment of interest, for any advances hereunder in any previous year remaining unpaid to it (with interest thereon at the rate of six per cent. per annum), the Cleveland Co. shall apply the balance of said net earnings and income to the payment of interest upon said Income Mortgage Bonds according to the requirements of the mortgage securing the same, and pay over to the Peoria Co. any amount thereof finally remaining. It is understood and agreed that the Cleveland Co. is to be entitled to make the customary charge for the use of any and all additional rolling stock and equipment furnished by it as hereinbefore provided for use on said lines of railroad from time to time, and that such charge shall form part of and be included in the expense of operation hereunder.

FOURTH.—Within sixty days after the 31st of December, 1890, and each year thereafter, the Cleveland Co. is to make up and state all its receipts for earnings and income from the said lines of railroad operated by it under these presents, and from said purchase money lien, and all its disbursements for interest or rental as aforesaid, and for the

cost and expense of using, operating and maintaining said lines of railroad and of complying with the requirements of these presents, and to render proper accounts thereof to the Peoria Co. and to the trustees of its said second mortgage as in said second mortgage required.

AND THESE PRESENTS FURTHER WITNESS THAT:

FIFTH.—The Cleveland Co. shall and will look only to such future net earnings of said lines of railroad operated by it under these presents and such future income of said purchase money lien, as shall not be required for the payment of said interest on said prior bonds and on said First Consolidated Mortgage Bonds, and hereinabove guaranteed by it, for the reimbursement to it of any sums it may advance in compliance with its aforesaid covenants and agreements, and the Peoria Co. hereby charges all such future net earnings and income coming to it, its successors or assigns, not required for the payment of said interest, with the payment of all such advances of the Cleveland Co., with interest upon said advances at the rate of six per cent. per annum.

SIXTH.—The Peoria Co. shall permit and suffer the use of its name by the Cleveland Co. in the use and operation of said lines of railroad, and in the acquisition of any and all property to be acquired for the purposes thereof.

SEVENTH.—Upon default by the Cleveland Co. in any act or thing by it to be done or performed under these presents, the Peoria Co., its successors or assigns, may resume the use and operation of its said lines of railway without prejudice to or impairment of the covenants and guaranty here-

inabove expressed. All personal or real property paid for out of the earnings or income of the Peoria Co. is to become and remain its property, and the Cleveland Co. undertakes that whenever this present contract or arrangement shall terminate, it shall and will restore to the Peoria Co. rolling stock and equipment adapted for use on its lines of railroad of at least the value of the rolling stock and equipment leased to it by these presents.

IN WITNESS WHEREOF, said parties hereto have caused their respective corporate seals to be to these presents affixed, and the same to be signed by their respective presidents and secretaries the day and year first above written.

THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY,

[SEAL] By M. E. INGALLS,
President.

Attest:
E. F. OSBORN,
Secretary.

THE PEORIA AND EASTERN RAILWAY CO.,

[SEAL] By J. A. BARNARD,
President.

Attest:
W. W. LYNN,
Secretary.

Signed and delivered in the presence of (as to The Cleveland, Cincinnati, Chicago & St. Louis Railway Company):

JOSEPH MOSES,
F. H. LOVETT.

Signed and delivered in the presence of (as to The Peoria and Eastern Railway Company):

FRANK J. RICHMANN,
EDWARD C. RUMPLER.

[Corporate acknowledgments omitted]

SUPPLEMENT TO OPERATING AGREEMENT— Dated February 22, 1890 (R. 23; Ex. 11)

THIS INDENTURE, made this twenty-second day of February, one thousand eight hundred and ninety, by and between THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY, party of the first part (hereinafter called the Cleveland Co.), and THE PEORIA AND EASTERN RAILWAY COMPANY, party of the second part (hereinafter called the Peoria Co.):

WHEREAS, The parties hereto by instrument of even date herewith, entered into a contract and arrangement for run-

ning the railroad of the Peoria Co., wherein and whereby, among other things, the Cleveland Co. guaranteed that the net earnings and income from the three sources in said instrument mentioned, actually applied to the payment of interest on the bonds therein mentioned, should not be less than four hundred and twelve thousand two hundred dollars in each and every year of the fifty years for which it thereby undertook the use and operation of the "Indiana part" of the line of railroad therein mentioned, and further agreed that such guaranty should be increased by the sum of forty dollars in each and every year for each and every one thousand dollars of the First Consolidated Mortgage Bonds therein mentioned in excess of $9,430,000, and also that it should and would look only to such future net earnings and income from said three sources as should not be required for the payment of said interest for the reimbursement to it of any sums it may advance in compliance with its covenants and agreements therein contained;

NOW, THESE PRESENTS WITNESS that the said parties hereto covenant and agree that, notwithstanding anything in said instrument or in the separate and independent covenant therein provided for contained, any and all sums of money provided or paid out by the Cleveland Co., or for its account, for the said interest over and above the actual net earnings as defined in Article Third of said instrument, and the actual net income from the purchase money lien therein mentioned, shall be deemed and taken to be an advance by the Cleveland Co. within the meaning of Article Fifth of said instrument as against all persons and parties whatsoever other than the holders of the First Consolidated Mortgage Bonds and the trustees of the mortgage securing the same; and that such is the true meaning and intent of the parties to said instrument.

IN WITNESS WHEREOF, the parties hereto have caused their respective corporate seals to be affixed to these presents, and the same to be subscribed by their respective presidents and secretaries as of the day and year first above written.

THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY,
[SEAL.] by M. E. INGALLS,
President.

Attest:
E. F. OSBORN,
Secretary.

Witness (as to E. F. Osborn, Secy.):
F. H. LOVETT,
EDWIN A. HILL.

THE PEORIA AND EASTERN RAILWAY COMPANY,
[SEAL.] by J. A. BARNARD,
President.

Attest:
W. W. LYNN,
Secretary.

Sealed and delivered in the presence of:

As to M. E. INGALLS, *Prest.*:
WALTER B. HORN,
BARRY MINES.

As to J. A. BARNARD, *Prest.* and W. W. LYNN, *Secy.*:
C. W. FAIRBANKS,
E. C. RUMPLER.

[Corporate Acknowledgments Omitted]

AGREEMENT—Dated April 1, 1940, Between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company and The Peoria and Eastern Railway Company, Extending the 1890 Operating Agreement (R. 23; Ex. 16)

AGREEMENT dated as of April 1, 1940, between THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY, hereinafter called the Big Four, party of the first part, and THE PEORIA AND EASTERN RAILWAY COMPANY, hereinafter called the Peoria and Eastern, party of the second part;

WHEREAS, by Indenture dated February 22, 1890 (which Indenture with supplement thereto of the same date is hereinafter called the Operating Agreement), the Peoria and Eastern did grant unto the Big Four, its successors and assigns, subject to the mortgage securing the Preferred Bonds of The Indiana, Bloomington and Western Railway Company in the aggregate principal amount of $1,000,000, and to the mortgage securing the Preferred Bonds of The Ohio, Indiana and Western Railway Company in the aggregate principal amount of $500,000, and to the First Consolidated Mortgage of the Peoria and Eastern securing its First Consolidated Mortgage Bonds for an aggregate principal amount not in excess of $10,000,000, the right to use and operate that portion of its railroad known as the Illinois part, extending from the Illinois-Indiana boundary line to the tracks of the Peoria and Pekin Union Railway Company, and its leasehold interest in that portion of its railroad known as the Indiana part, extending from the Illinois-Indiana boundary line to the tracks of the Indianapolis Union Railway

Company, and all the rolling stock and equipment of the Peoria and Eastern (included as part of the Indiana part) as more particularly provided in the Operating Agreement for and during the period of fifty years from April 1, 1890 and such further time thereafter as the Big Four might elect to use and operate said Indiana part and said Illinois part of the railroad of the Peoria and Eastern upon the terms, covenants and agreements contained in said Indenture; and

WHEREAS, the Preferred Bonds of The Ohio, Indiana and Western Railway Company, in the aggregate principal amount of $500,000 above referred to, matured on April 1, 1938 and were paid at maturity through moneys borrowed by the Peoria and Eastern upon its promissory note maturing April 1, 1940 and secured by the pledge, among other securities, of $500,000, principal amount, of First Consolidated Mortgage Bonds issued under the First Consolidated Mortgage in exchange for the bonds of The Ohio, Indiana and Western Railway Company so maturing; and

WHEREAS, in view of the maturity on April 1, 1940 of the Preferred Bonds of The Indiana, Bloomington and Western Railway Company and of the First Consolidated Mortgage Bonds and of the said promissory note of the Peoria and Eastern, the Peoria and Eastern prepared a Plan of Adjustment under Article XV of the Bankruptcy Act, dated January 10, 1940, hereinafter called the Plan, which Plan was finally approved and confirmed by the Court having jurisdiction of the subject matter thereof on or about the 29th day of July, 1940; and

Operating Agreement Extension—April 1, 1940

WHEREAS, the Plan as confirmed and approved as aforesaid provides for the execution of an agreement between the Big Four and the Peoria and Eastern evidencing the election made by the Big Four to continue to use and operate the said Illinois part and the said Indiana part of the railroad of the Peoria and Eastern during the period from April 1, 1940 to April 1, 1960 under the terms of the Operating Agreement as amended in accordance with the Plan:

NOW, THEREFORE, THIS AGREEMENT WITNESSETH:

That the parties hereto for the purpose of evidencing the election made by the Big Four to continue to operate the Indiana part and the Illinois part of the railroad of the Peoria and Eastern for the extended term of twenty years from April 1, 1940 to April 1, 1960, as provided in the Plan, do hereby confirm and acknowledge the election made by the Big Four as aforesaid and agree as follows:

FIRST: That pursuant to the election of the Big Four as aforesaid, the term of the Operating Agreement shall continue for the additional period from April 1, 1940 to April 1, 1960, subject to all the terms, covenants, conditions and agreements contained in the Operating Agreement; except that in view of

(a) The payment of the purchase money lien of $5,000,000, reserved and declared in the deed dated February 22, 1890 made by Charles H. Coster and Samuel Spencer to the Big Four of that part of the railroad formerly of The Ohio, Indiana and Western Railway Company extending from Springfield, Ohio, to Indianapolis, Indiana, and

(b) The payment of the Preferred Bonds of The Indiana, Bloomington and Western Railway Company and the Preferred Bonds of The Ohio, Indiana and Western Railway Company and the reduction of the aggregate principal amount outstanding of the First Consolidated Mortgage Bonds of the Peoria and Eastern to $4,722,300, with maturity date extended to April 1, 1960, without change in the interest rate,

the amount of the deficiency which under Clause Second of the Operating Agreement the Big Four was obligated to provide for and make good in the fund necessary for the due and punctual payment of the interest as it accrued on the two issues of Preferred Bonds above referred to (so paid) and on the First Consolidated Mortgage Bonds of the Peoria and Eastern (so reduced in principal amount and with maturity date extended) and of any tax or taxes which the Peoria and Eastern might be required to pay or retain from the interest on said bonds, shall during such extended term of the Operating Agreement, be such amount as may be required for the due and punctual payment of the interest as it accrues on the aggregate principal amount from time to time outstanding of the First Consolidated Mortgage Bonds of the Peoria and Eastern (not to exceed $4,722,300 principal amount), and of any tax or taxes which the Peoria and Eastern may be required to pay or retain from the interest on said Bonds; and the guaranty with respect to interest expressed in said Clause Second is modified so that the Big Four shall, and hereby does, guarantee that, during such extended term of the Operating Agreement, the net earnings derived from the Indiana part and the net earnings derived from the Illinois part of the line of railroad of the Peoria

and Eastern actually applied to the payment of interest on said First Consolidated Mortgage Bonds of the Peoria and Eastern (so reduced in principal amount and with maturity date extended), as above provided, shall not be less than the amount required to pay such interest in full as it becomes due in each and every year of such extended term, and the covenants of said Clause Second of the Operating Agreement as modified hereby and the foregoing guaranty shall be deemed and taken to be a direct and absolute obligation and guaranty of the Big Four to the trustee under the mortgage securing said extended First Consolidated Mortgage Bonds and to all and singular the persons and parties, who may at any time be or become the holders of said extended Bonds or any of them, for the payment of all the interest to accrue thereon during such extended term, as and when it shall become payable.

SECOND: That during the continuance of the lease dated January 2, 1930 whereby the Big Four leased its lines of railroad and other property to The New York Central Railroad Company, The New York Central Railroad Company, as provided in said lease and subject to the terms and provisions thereof, shall continue to operate and use the Illinois part and the Indiana part of the railroad of the Peoria and Eastern during the extended term herein provided for under and in accordance with the terms of the Operating Agreement, as extended and modified hereby.

THIRD: That the Big Four will replace or cause to be replaced the equipment of the Peoria and Eastern which has been retired and not replaced or has become unserviceable for further use, with suitable equipment or additions

and betterments to equipment equal in value to the cost to the Peoria and Eastern of such retired or unserviceable equipment as the same appears upon the books of the Peoria and Eastern, and that during the extended term of the Operating Agreement it will replace annually any equipment that may during the year have been retired or become unserviceable for further use with suitable equipment or additions and betterments to equipment equal in value to the cost to the Peoria and Eastern of such retired or unserviceable equipment as the same appears upon the books of the Peoria and Eastern. It is understood and agreed, however, that all expenditures in connection with such replacement and additions and betterments shall be charged against the equipment retirement account at that time held by the Big Four or its lessee, The New York Central Railroad Company, for the Peoria and Eastern.

In Witness Whereof, the parties hereto have caused this agreement to be executed this 18th day of November, 1940.

The Cleveland, Cincinnati, Chicago and St. Louis Railway Company,

[Corporate Seal]

By F. E. Williamson,
President.

Attest:

B. H. Sheffer,
Assistant Secretary.

Signed, sealed and delivered as to THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY in the presence of:

E. W. JORDAN
F. A. GROGAN

THE PEORIA AND EASTERN RAILWAY COMPANY,

[CORPORATE SEAL]

By W. F. PLACE,
Vice-President.

Attest:

J. M. O'MAHONEY,
Secretary.

Signed, sealed and delivered as to THE PEORIA AND EASTERN RAILWAY COMPANY in the presence of:

F. T. FLANAGAN
F. A. GROGAN

[Corporate Acknowledgments Omitted]

INCOME MORTGAGE—Dated February 22, 1890, From Peoria and Eastern Railway Company to Central Trust Company and Charles W. Fairbanks, Trustees (R. 23; Ex. 13)

THIS INDENTURE, made this twenty-second day of February, one thousand eight hundred and ninety, by and between THE PEORIA AND EASTERN RAILWAY COMPANY, a corporation, organized and existing under the laws of the State of Illinois, party of the first part (hereinafter called the Railway Company), and THE CENTRAL TRUST COMPANY OF NEW YORK, a corporation organized and existing under the laws of the State of New York, and CHARLES W. FAIRBANKS, of Indianapolis, Indiana, parties of the second part (hereinafter called the trustees), WITNESSETH:

Income Mortgage—February 22, 1890

WHEREAS, the Railway Company, being authorized and empowered by law to purchase, own, operate and maintain any railroad sold or transferred under order or powers of sale, or decree of, or sale under, foreclosure of mortgage or deed of trust, has purchased, and now owns and intends to operate and maintain the railroad hereinafter mentioned, which was recently sold under foreclosure of mortgages therein created by former owners thereof;

AND, WHEREAS, the Railway Company proposes to pay the price of its said purchase in part by the issue and delivery of the four million dollars of income bonds in these presents provided for and in part by the delivery of other securities; and to mortgage its corporate property, whether held in fee or by leasehold or otherwise, and the franchises to such property appertaining, to secure the payment of said bonds; said bonds to be of even date with these presents, for an aggregate amount of four million dollars and for $1,000 each, payable on the first day of January, in the year one thousand nine hundred and ninety-one, with interest thereon at a rate not exceeding four per cent. in any one year, payable in accordance with coupons therefor to be annexed to said bonds, but only out of the net earnings and income of the Railway Company as the same shall be ascertained for each particular year, beginning with the year ending December 31, 1890, in the manner provided in these presents, such interest to be absolutely non-cumulative. The principal and interest of said bonds are to be paid at the office or agency of the Company in the City of New York. Said bonds are to be numbered consecutively from No. 1 upwards, and are to be substantially in the form following:

Income Mortgage—February 22, 1890

No... UNITED STATES OF AMERICA, $1,000

STATE OF ILLINOIS.

Income Mortgage Four Per Cent. Non-Cumulative Bond of the Peoria and Eastern Railway Company. Principal payable April 1, 1990 Interest when earned payable April 1st.

KNOW ALL MEN BY THESE PRESENTS, that the Peoria and Eastern Railway Company is indebted to the Central Trust Company of New York, in the sum of one thousand dollars, which sum said Railway Company promises to pay to the bearer hereof on the first day of April, one thousand nine hundred and ninety, with interest thereon from April 1, 1890, at a rate not exceeding four per cent. in any one year, payable in accordance with the coupons therefor hereto annexed, but only out of the net earnings and income of said Railway Company, as the same shall be ascertained for each particular year, beginning with the year ending December 31, 1890, in the manner provided in the mortgage hereinafter mentioned, and which interest, it is distinctly understood, shall be absolutely non-cumulative. The principal and interest of this bond are to be paid at the office or agency of the company in the City of New York.

This bond is one of a series aggregating $4,000,000 mentioned in and all equally and without preference of one over the other secured by a certain Income mortgage of even date herewith executed by said

Railway Company to said Central Trust Company and Charles W. Fairbanks, as trustees of and upon the railroad and other property of said Railway Company, and it shall become obligatory upon said Railway Company, only when authenticated by the certificate of said Trust Company as such trustee endorsed hereon.

IN WITNESS WHEREOF, said Railway Company has caused its corporate seal to be affixed to these presents and the same to be subscribed by its President and Secretary this twenty-second day of February, one thousand eight hundred and ninety.

[SEAL] .....*President.*

.....*Secretary.*

(INTEREST COUPON)

The Peoria and Eastern Railway Company will pay to the bearer hereof, at its office or agency in the City of New York, on the 1st day of April , such sum, if any, and not exceeding $, as shall have been ascertained as the amount payable out of the net earnings and income of said Railway Company for the year ending the previous 31st of December, upon its Income Mortgage Bond No.

.....*Treasurer.*

(The coupons maturing April 1, 1891, shall read for $30, and the coupons maturing annually thereafter shall read for $40 each.)

(TRUSTEE'S CERTIFICATE)

This bond is one of the series of Income Mortgage Bonds of the Peoria and Eastern Railway Company issued under and secured by the mortgage executed to the undersigned and Charles W. Fairbanks by said Railway Company dated February 22, 1890, and within referred to.

CENTRAL TRUST COMPANY OF NEW YORK,

by.....

Vice-President.

AND WHEREAS, pending the engraving and delivery of bonds in the form above set forth, the Railway Company proposes to issue and deliver one temporary bond for $4,000,000, to be certified by the Central Trust Company of New York, one of the trustees, as above provided, and to be of the same general substance as the form above set forth, but without coupons, the payment of interest thereon, when and as made, to be endorsed thereon, which said temporary bond for $4,000,000 shall be exchanged for bonds of $1,000 each in the form above set forth, and said temporary bond shall then be canceled, but in the meanwhile said temporary bond for $4,000,000 shall have the security of these presents.

AND WHEREAS, by a vote of the stockholders of the Railway Company at a meeting of them duly called and held before the execution of these presents, the concurrence in the making of this mortgage of the holders of more than two-thirds of said capital stock was expressed in the manner prescribed by law;

NOW, THEREFORE, THESE PRESENTS WITNESS, that the Railway Company, in consideration of the premises and of one dollar to it in hand paid by the trustees, the receipt whereof is hereby acknowledged, has granted, bargained and sold, and by these presents doth grant, bargain and sell to the trustees all of the Railway Company's right, title and interest, whether now held or hereafter to be acquired, of, in and to the part of the railway lately of the Ohio, Indiana and Western Railway Company, extending from Pekin, Illinois, to the tracks of the Indianapolis Union Railway Company, at or near Indianapolis, Indiana, and all and singular its right to use the tracks and certain other property of said Indianapolis Union Railway Company and of the Peoria and Pekin Union Railway Company, and its rights and interest therein, and all road-bed, embankments, trestles, culverts, bridges and their approaches, railroad tracks and the lands upon which the same stand, stations, station grounds, engine houses, shops, yards, side tracks, turn-tables, switching and signaling apparatus, rights of way, easements and privileges forming or constituting any part of the aforesaid railway, and all franchises appertaining thereto, and all engines, cars, coaches and other rolling stock, and all tools, implements and other movable equipment and supplies for use on the aforesaid railway, and all appendages and appurtenances now used or to be hereafter acquired for use in connection with the aforesaid railway in any manner whatsoever, the same being subject to prior liens thereon, as follows:

(1) A mortgage dated April 15, 1879, executed by the Indiana, Bloomington and Western Railway Company to the Central Trust Company of New York, to secure the payment of its bonds to the amount of $1,000,000; and

(2) A mortgage dated April 2d, 1889, executed by the Ohio, Indiana and Western Railway Company to the Central Trust Company of New York, to secure the payment of its bonds to the amount of $500,000.

And also all the right, title and interest of the Railway Company of, in and to a certain purchase-money lien and charge $5,000,000 and the income thereof on the part of the railway late of the Ohio, Indiana and Western Railway Company extending from Springfield, Ohio, westward to the tracks of the Indianapolis Union Railway Company, declared and reserved in and by the deed thereof to the Cleveland, Cincinnati, Chicago and St. Louis Railway Company, dated February 22, 1890, and all the right, title and interest of the Railway Company of, in and to the premises so conveyed, the same being also subject to the said prior lien thereon created by said mortgage executed by the Ohio, Indiana and Western Railway Company, dated April 2d, 1888, to secure the payment of its said bonds to the amount of $500,000.

The entire railway and property conveyed by these presents are subject to a further lien thereon, also prior and superior to the lien of these presents, created by the Railway Company by its first mortgage of even date herewith, to said parties of the second part as trustees, for the security of $10,000,000 of its First Consolidated Mortgage Bonds, and it is intended that these presents shall at all times be subject to the prior and superior lien of the last mentioned mortgage and of said First Consolidated Mortgage Bonds and of any and all extensions and renewals thereof however effected, and of the principal and interest of any new series of bonds not exceeding the amount of said First Consolidated Mortgage Bonds at the time of

such new issue outstanding, and bearing interest at no higher rate than four per cent. per annum, and of the mortgage to be given to secure such new series of bonds, and subject to the right to extend the time of payment of said purchase-money lien for the period covered by any such extension of said First Consolidated Mortgage Bonds, or by any such new series of bonds, and also subject and subordinate to a certain contract made by the Railway Company with the Cleveland, Cincinnati, Chicago and St. Louis Railway Company, dated February 22, 1890.

To have and to hold the same to the trustees, their successors and assigns, in trust and for the equal benefit and security of the holders of the bonds of the Railway Company of the series hereby secured and without preference of one over the other, and upon the terms and conditions following, that is to say:

First.—That until default in the payment of any interest of the bonds hereby secured or of any of them according to the terms of the coupons annexed to said bonds and of this mortgage, or in the payment of the principal of said bonds or any of them, or until default by the Railway Company in some covenant, promise or agreement on its part to be kept or performed pursuant to these presents, it shall possess, use and enjoy the premises hereinabove mortgaged and receive the rents, issues and profits thereof.

Second.—That if the Railway Company, its successors or assigns, shall at any time hereafter make default, or refuse, neglect or omit for any period exceeding three months to pay the annual interest on the bonds hereby secured, or any of them, according to the tenor of the

coupons annexed to said bonds and of this mortgage, or if, after the principal of said bonds shall have become due and payable, as in these presents or in said bonds provided, the Railway Company shall make default or refuse, neglect or omit to pay the principal of each and all of the said bonds, or shall for any period exceeding three months refuse or fail to keep or perform any of the covenants, promises or agreements contained in these presents or in said bonds, on its part to be kept or performed, then and in every such case (1) the trustees shall and will, upon the written request of holders of one-quarter in amount of said bonds then outstanding, and upon adequate security and indemnity against all costs, expenses and liabilities to be by the trustees incurred, or within such request, or security or indemnity, in their own discretion, the trustees may forthwith demand, and with such force as may be necessary, enter, take and maintain possession of all and singular the railways and other property hereby conveyed and mortgaged, or intended so to be, and as the attorney in fact, or agent of the Railway Company in person, or by agents and substitutes duly constituted, or by their managers, superintendents, receivers, or servants, have, hold, use, manage, operate, lease, and enjoy the same, and each and every part thereof, to as full an extent as the Railway Company might lawfully do, making from time to time all needful and proper repairs, alterations and additions, and receiving all the tolls, incomes and revenues thereof, and after deducting the expenses of such use, operation, reasonable repairs, alterations and additions, and taxes, assessments, insurance and other proper charges on the said railroad or the appurtenances or other property or any part thereof, and the costs and charges of such taking possession, and proper compensation for their services for such taking

possession and management while in possession, and such sum or sums as may be sufficient to indemnify the trustees against any liability, loss or damage for or on account of any matter or thing done in good faith, in pursuance of the duties of the trustees, shall apply the remaining net income and revenue therefrom to the payment of the interest accrued and accruing on the said bonds outstanding and intended to be hereby secured to the persons or parties holding the coupons therefor, or entitled to receive the same, without any discrimination or preference between them; (2) or the trustees shall and will, after or without entering upon or taking possession, upon the written request of holders of a like amount of said bonds then outstanding, and upon like security and indemnity, or without such request or security or indemnity, in their own discretion, the trustees may proceed to sell and dispose of all and singular the said railway and other property hereby mortgaged, or intended so to be, to the highest and best bidder, at public auction at such place on the line of the said railways as the trustees may designate, and at such time as they shall appoint, having first given notice of the place and time of such sale by advertisement published not less than twice each week for six weeks in one or more newspapers in the City of New York, in Indianapolis and in Peoria aforesaid, or to adjourn the said sale from time to time, in their discretion, and if so adjourning, to make the said sale at the time and place to which the same may be adjourned; and to make and deliver to the purchaser or purchasers of the said railways and other property hereby mortgaged, good and sufficient deeds or conveyances therefor, freed from all and every the trusts hereby created, and without liability on the part of the purchaser to see to the application of the purchase money, or to inquire into the necessity, expediency or authority of

or for any such sale; which sale, made as aforesaid, shall be a perpetual bar, both in law and in equity, against the Railway Company and all persons claiming or to claim the said railway and other property, or any part thereof, or any interest therein, by, from, or through the Railway Company; and after deducting from the proceeds of such sale proper allowances for all expenses thereof, including attorney and counsel fees, and all other expenses, advances or liabilities which may have been made by the trustees for taxes or assessments, or other proper charges on the said railways and other property, or any part thereof, as well as reasonable compensation for their own services, it shall be lawful for the trustees, and it shall be their duty, to apply the residue of the money arising from the said sale to the payment of the principal of such of said bonds as shall be then outstanding and of the interest which shall have accrued on the said principal up to that time, without distinction or preference as between principal and interest, but ratable to the aggregate amount of such principal and accrued interest, it being understood and hereby declared that such payments shall be made to the persons holding the bonds and coupons secured hereby, evidencing the right to such principal and interest without discrimination or preference between them; and in the event of there being in the hands of the trustees any portion of the railway and other property, hereby mortgaged or intended so to be, or the proceeds thereof, after the payment in full of the interest and principal of the aforesaid bonds, then the trustees shall reconvey, retransfer or pay over the same to the Railway Company, its successors or assigns, for its sole use and benefit; (3) or the trustees shall and will, after, or without, entering upon or taking possession, upon the written request of holders of a like amount of said bonds then out-

standing, and upon like security and indemnity, or without such request or security or indemnity, in their own discretion, the trustees may proceed to protect and enforce the rights of the holders of said bonds under these presents, by a suit or suits in equity or at law, either for the specific performance of the stipulated covenants and agreements, or any of them, contained herein, or in aid of the execution of powers herein granted, or for the foreclosure of this mortgage, or for the enforcement of any other appropriate legal or equitable remedy as the trustees, being advised by counsel learned in the law, shall deem most effectual to protect and enforce such rights, and in all such proceedings for the enforcement of these presents, the said purchase money lien hereinabove conveyed shall constitute part of the mortgaged premises and may be sold with the other property hereby conveyed or separately therefrom, as the trustees may deem expedient and shall elect.

No holder or holders of a bond, or of any bonds or coupon or coupons secured hereby, shall have the right to institute any suit, action or proceeding in equity or at law for the foreclosure of these presents, or the execution of the trusts thereof, or for the appointment of a Receiver, or for the recovery at law of the principal or interest of any of said bonds or of any part of said principal or interest, or for the ascertainment of the net income applicable to the payment of interest on any of the bonds secured hereby, or for any other remedy, without having first given notice in writing to the trustees of the fact that default has occurred and continued as aforesaid, and making request in writing to the trustees, and having afforded them a reasonable opportunity to proceed to exercise the powers hereinbefore granted, or to institute such action, suit or pro-

ceeding in their own name, and having also offered to them adequate security and indemnity against the cost, expenses and liabilities to be incurred therein or thereby; and such notification, request and offer of indemnity are hereby declared to be conditions precedent to any action, or cause of action, by any holder or holders of said bonds, for the recovery at law of the principal or interest of any of said bonds or of any part of said principal or interest, or for the ascertainment of the net income applicable to the payment of interest on any of the bonds secured hereby, or for the foreclosure of these presents, for the appointment of a Receiver, or for any other remedy hereunder, it being intended that no one or more holders of bonds or coupons shall have the right in any manner whatever to affect, disturb or prejudice the lien of this mortgage by his or their action, except in the manner herein provided.

THIRD.—That in the event of default in the payment of interest as aforesaid, or in the performance of any of the covenants, promises and conditions contained herein, made and continuing as hereinbefore mentioned, or in the event of the trustees making entry upon or taking possession of the railway and other property and franchises hereby mortgaged, or agreed or intended so to be, then and in either such case the whole principal sum of each and all of the said bonds then outstanding, and intended to be hereby secured, shall, at the option of the trustees, or if the trustees omit to declare the principal due, at the option of the holders of twenty-five per cent. in the amount of the bonds then outstanding, expressed in writing under their hands, and delivered to the trustees, forthwith become due and payable, and in case of a sale of the mortgaged premises, either by the trustees or in consequence of judicial proceed-

ings, the whole of said principal sum shall at once become due and payable if the same shall not have been previously declared due, anything in said bonds or herein contained to the contrary notwithstanding; but when the principal sum thereof has been declared to be due and payable by the trustees, the holders of a majority in amount of said bonds then outstanding may instruct the trustees to waive the right so to declare or may annul or reverse such declaration on such terms and conditions as such holders of bonds may deem proper, but no such action of the trustees or holders of bonds shall affect any subsequent default or impair any rights resulting therefrom.

FOURTH.—That in any and every proceeding for the enforcement of these presents, the trustees shall be entitled as a matter of right to a receivership of the mortgaged premises, and of the rents, issues and profits thereof, and in any and every such proceeding the Railway Company shall surrender and waive, and hereby does surrender and waive, the benefit of any exemption, stay or appraisement laws now existing or which may hereafter exist in respect of any part of said railways and other property; and that upon any sale of the mortgaged premises, or any part thereof, in enforcement of these presents, the bonds hereby secured and the interest coupons thereof shall be receivable in payment of the price to be paid by the purchaser to the extent that the same shall or would confer a right to the proceeds of such sale; and that no delay or omission of the trustees, or of the holders of the bonds hereby secured to exercise any of the rights and powers given to them, or either or any of them, by these presents, shall be held to impair or defeat said rights and powers, or any of them, or be construed or taken to be a waiver of them, or of any

of them, or an acquiescence in any default upon which the same may arise.

AND THESE PRESENTS FURTHER WITNESS:

FIFTH.—That the Railway Company shall and will promptly apply the net earnings and income, to be ascertained as herein provided, to the payment of all interest upon all of said series of prior bonds hereinabove mentioned, as and when the same shall become payable, according to the terms and conditions herein prescribed and not otherwise; and also shall and will pay all taxes, assessments or other like charges lawfully laid or charged upon the mortgaged premises, or any part thereof, which may or might impair the priority of lien of these presents. In case the Railway Company shall make default in paying any such taxes, assessments or other like charges, the trustees or any holders of bonds of the series hereby secured may advance the amount required for the purpose of such payment, and have a first lien upon the mortgaged premises and any proceeds thereof for their reimbursement, but nothing herein contained shall impose any duty or obligation upon the trustee to see to the performance by the Railway Company of its covenants to pay taxes, assessments or other like charges, except at the request of holders of bonds of the series hereby secured, accompanied by a deposit of money to the amount necessary for the purpose.

SIXTH.—That beginning with the year ending December 31, 1890, the Board of Directors of the Railway Company shall ascertain and declare the net earnings and income applicable to the payment of interest upon the bonds

secured hereby for the year ending the 31st day of December in each year, by deducting from the gross earnings and income of the Railway Company for such year all interest on prior bonds, and on said First Consolidated Mortgage Bonds, expenses of operation and maintenance, taxes, assessments, insurance, rentals and other like charges, cost of repairs, renewals and reasonable betterments to the property of the Railway Company necessary for its economical and efficient operation, and all deficiencies arising from payments for said purposes in former years not otherwise provided for and all advances which shall have been made to provide for such deficiencies or any part of them, and shall apply such net earnings and income (or such portion thereof as may be necessary) towards payment of the interest on the bonds hereby secured, in accordance with their terms and the provisions hereof. The said net earnings and income of each year shall be ascertained and declared by the Directors not later than the 1st day of March following each 31st day of December, and the interest declared by them shall be paid on the first day of April following.

The Railway Company shall on or before the first day of March of each year furnish the trustees with a statement showing the amount of the net earnings and income of the previous year so ascertained and declared to be applicable to the interest on the bonds secured by this mortgage, and give public notice of the rate of interest payable on said bonds. If the trustees shall not be satisfied with the said statement, or if said trustees shall be notified in writing by the holders of bonds to the amount of one-fifth of the amount outstanding that they object to the same within thirty days after the same shall have

been received by the trustees, it shall be the duty of the said trustees forthwith to notify the Railway Company of such objection. And the trustees shall have the right to inspect the books of the Railway Company by a proper officer of said Central Trust Company of New York, or by an expert accountant appointed for the purpose (such appointment to be made by said Trust Company so long as it shall continue as one of the trustees hereunder), who shall be paid for his services by the Railway Company.

If the said difference for any reason shall not be adjusted by agreement between the trustees and the Railway Company, or if the trustees be called upon to proceed by the holders of one-fifth of the amount of bonds outstanding secured by this mortgage, who shall also have duly indemnified the trustees against all liability for costs and expenses, then and in that event it shall be lawful for and the duty of the trustees to file a bill in equity against the Railway Company in any court of competent jurisdiction, for an account of the net earnings and income under the provisions of this mortgage, and if it shall be adjudged in such action that there are such net earnings and income available, under the terms of this mortgage, for the purpose of paying the interest on the bonds secured by this mortgage beyond the amount declared in the statement so furnished by the Railway Company, then, unless the Railway Company shall, within three months after such adjudication, pay the said balance of the net earnings and income so adjudged to be available by way of interest to the holders of the bonds hereby secured, such non-payment shall constitute a default in the payment of interest, for which the trustees shall be authorized to pro-

ceed under the terms of the second, third and fourth articles of this mortgage. The remedy herein provided for ascertaining the amount of the net earnings, in case of dispute, shall be exclusive of all other proceedings, actions, suits, and demands whatsoever.

SEVENTH.—That so long as any of the bonds of the series hereby secured shall remain outstanding, the Railway Company covenants that it shall and will keep open and maintain an office or agency at the city of New York, where the interest and principal of said bonds shall be paid; and that in case, at the maturity of said bonds, any holders of the same shall not present the same for payment and receive payment thereof for thirty days after the same shall have matured, the Railway Company shall have the right to deposit the moneys due thereon with said Central Trust Company, as trustee, and in trust for the holders of said bonds, and thereby satisfy and discharge all their lien or right under these presents.

EIGHTH.—That if at any time any property, real or personal, forming part or parcel of the mortgaged premises shall be or become no longer required for use in the operation of said railroad and by the Railway Company shall be declared so to be, the trustees may, if in their judgment the security of the holders of the bonds hereby secured be not thereby substantially impaired, release the same from this mortgage.

NINTH.—That the trustees, or either of them, may resign by notice in writing to the Railway Company or its successors in interest, or after default under these presents by the Railway Company may be removed by writing signed

by the holders of a majority of the bonds of the series hereby secured at the time outstanding and delivered to the trustees, and in either case thereupon a successor to said parties of the second part or either of them in the trusts of these presents may be appointed either by writing signed by the holders of a majority of the bonds of said series at the time outstanding and delivered to the Railway Company or its successors in interest, or by any competent court upon application of the holder or holders of not less than one-tenth in amount of the bonds of said series at the time outstanding, and after such notice to the holders of the other bonds of said series as said court shall direct. Each and every such appointment or substitution trustees shall be a valid and sufficient transfer and assignment of the mortgaged estate to the new or incoming trustee and of these presents and of all property held thereunder. No trustee shall be held liable except for its or his own willful default, neglect or misfeasance, and the word "trustees" as used in these presents shall be taken to include not only said party of the second part, but also all persons and parties who shall at any time become or be trustees of this mortgage. The trustees shall be entitled to reasonable compensation for all services they may render in the execution of the trusts of this mortgage to be paid by the Railway Company and its successors and for which the trustees shall have a lien on the property mortgaged.

TENTH.—That in each and every case herein mentioned of writings to be signed by the holders of bonds of the series hereby secured the signature and assertion of ownership thereof shall be adequately proved by the certificate of a notary public or other public officer authorized to take acknowledgments or to administer oaths, of the acknowledg-

ment of the signature accompanied by declaration of ownership, and such writings may be in separate copies and parts and separately signed.

ELEVENTH.—That the Railway Company covenants, promises and agrees to and with the trustees, their successors, and assigns, that, in consideration of the premises, it, the Railway Company, shall and will stand seized and possessed of any and all property, real or personal, rights or franchises, which it now holds or hereafter shall or may acquire, as part of or for use in connection with the railroad hereby mortgaged, or any part thereof, in trust and subject to the terms, covenants and conditions of these presents, and that it, the Railway Company, and its successors, shall and will from time to time, and at all times hereafter, execute and deliver all such other or further conveyances or assurances as may be reasonably advised, devised or required by the trustees or their counsel learned in the law for the better assuring unto the trustees of the premises hereby mortgaged and every part thereof, whether now held or hereafter to be acquired.

TWELFTH.—That the trustees signify their acceptance of the trusts created in and by these presents by joining in the execution hereof.

IN WITNESS WHEREOF, the Railway Company and the said Trust Company have caused their respective corporate seals to be hereunto affixed, and the same to be subscribed by their respective presidents or vice-presidents and secretaries, and the said Fairbanks has hereunto set his hand and seal the day and year first above written.

NOTE: Page 3, line 21, the words "$30" written over an erasure; page 7, line 6, after the words "these presents" the words "or in said bonds" interlined before execution hereof. In the presence of, as to P. & E. R. Co. and Fairbanks.

C. E. TRACY,
C. H. COSTER,
O. A. MCFARLAND

THE PEORIA AND EASTERN RAILWAY CO.,
[SEAL] By J. A. BARNARD,
President.

W. W. LYNN,
Secretary.

CENTRAL TRUST COMPANY OF NEW YORK,
[SEAL] By F. P. OLCOTT,
President.

Attest:
C. H. P. BABCOCK,
Secy.

Witness:
G. SHERMAN,
M. FERGUSON.

C. W. FAIRBANKS [SEAL]

[Corporate Acknowledgments Omitted]

Supplement to Income Mortgage—Dated March 25, 1890 from Peoria and Eastern Railway Company to Central Trust Co. and Charles W. Fairbanks, Trustees (R. 23; Ex. 13)

THIS INDENTURE, made this twenty-fifth day of March, one thousand eight hundred and ninety, by and between THE PEORIA AND EASTERN RAILWAY COMPANY, party of the first part (hereinafter called the Railway Company), and and CENTRAL TRUST COMPANY OF NEW YORK, and CHARLES W. FAIRBANKS, of Indianapolis, Indiana, parties of the second part (hereinafter called the trustees), WITNESSETH:

WHEREAS, the Railway Company heretofore executed and delivered to the trustees its certain Income Mortgage, dated the 22d of February, 1890, wherein and whereby it mortgaged to the trustees its railroad and other property, subject to certain prior mortgages thereon, and in particular to its First Consolidated Mortgage of even date therewith, and also subject and subordinate to a certain contract made by the Railway Company with the Cleveland, Cincinnati, Chicago and St. Louis Railway Company, dated February 22, 1890, in trust to secure the payment of a certain series of $4,000,000 of said Railway Company's Income Mortgage Bonds, of even date therewith;

AND WHEREAS, the Cleveland, Cincinnati, Chicago and St. Louis Railway Company and the Railway Company have executed a supplement to said contract bearing date the 22d day of February, 1890;

NOW, THEREFORE, THESE PRESENTS WITNESS that the parties hereto grant, covenant and agree to and with each other that the said Income Mortgage is amended as follows:

Supplement to Income Mortgage—March 25, 1890

1. The form of said Income Bonds therein set forth is amended by adding in the paragraph thereof describing the Income Mortgage securing the same, and after the words "of and upon the railroad and other property of said Railway Company," the words: *"and an indenture supplemental thereto dated March 25, 1890;"* and by adding in the trustee's certificate therein set forth, after the words "dated February 22, 1890," the words: *"and the indenture supplemental thereto dated March 25, 1890."*

2. The description of the mortgaged premises therein contained is amended by adding at the end of the paragraph, setting forth the liens and charges to which the same are subject, the words: *"and a supplement thereto of even date therewith."*

AND THESE PRESENTS FURTHER WITNESS that the parties hereto further grant, covenant and agree to and with each other that, for all purposes whatsoever, the foregoing amendments and additions shall be deemed and taken to be part and parcel of the said Income Mortgage, and to have the same force and effect as if the same had been originally incorporated in said Income Mortgage, and also that bonds only of the amended form and tenor hereinbefore provided for, and of no other form and tenor, shall be issued and certified as being of the series of Income Mortgage Bonds secured by said Income Mortgage.

IN WITNESS WHEREOF, the Railway Company and the said Trust Company have caused their respective corporate seals to be affixed to these presents, and the same to be subscribed by their respective presidents or vice-presidents

and secretaries, and the said Fairbanks has hereunto set his hand and seal the day and year first above written.

THE PEORIA AND EASTERN RAILWAY CO.,
[SEAL] By J. A. BARNARD,
President.

Attest:
W. W. LYNN,
Secretary.

CENTRAL TRUST COMPANY OF NEW YORK,
[SEAL] By E. FRANCIS HYDE,
2d Vice President.

Attest:
C. H. P. BABCOCK,
Secretary.

C. W. FAIRBANKS. [SEAL]

Sealed and delivered in the presence of

As to P. & E. Ry. Co. and C. W. Fairbanks.
E. C. RUMPLER,
FRANK J RICHMANN.

As to Central Trust Co. of New York.
T. STALLKNECHT,
I. S. ROBINSON.

[Corporate Acknowledgments Omitted]

Extract From Minutes of Meeting of Board of Directors of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, July 24, 1889 (R. 23; Ex. 20)

Whereas the officers of the Ohio, Indiana and Western Railroad Company have approached this Company with a view of making some arrangements by lease or otherwise of the property contracted by them, therefore be it

Resolved, that the question be referred to a Committee, consisting of the President, Vice President, Messrs. C. Vanderbilt and J. Pierpont Morgan, to conduct such negotiations with power to execute, if a satisfactory arrangement can be made.

Extract From Minutes of Meeting of Board of Directors of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, September 18, 1889 (R. 23; Ex. 21)

The President offered the following report of Committee on Ohio, Indiana & Western purchase.

The Committee report that they have substantially arranged with the O. I. & W. people to take said road and operate it on the following basis, to wit:

From October 1st to December 31st, 1889 the earnings to be applied to the payment of the floating debt; from Jany. 1st, 1890 on, the fixed charges of the road to be reduced to $412,740 a year, and in case the net earnings of the road in any year should not amount to that sum, the Cleveland, Cincinnati, Chicago & St. Louis Ry. Co. to loan the deficit, to be

repaid out of any excess over and above that sum in future years.

In consideration of this, one half of the $10,000,000 of capital stock is to be given.

Whereupon, on motion of Mr. Anderson, seconded by Mr. Townsend, it was

Resolved, that the report of the Committee be approved by the Board and the Committee given full power to act.

Extract From Minutes of Meeting of Board of Directors of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, October 29, 1889 (R. 23; Ex. 22)

The matter of contract with the Reorganization Committee of the Ohio, Indiana & Western Ry. Co., was discussed and a rough draft of a proposed contract together with sketch of reorganization agreement and of papers incidental thereto, was submitted and discussed.

The Vice Prest. stated that it was expected that the contracts would, in a short time, be in final shape for execution. The sense of the meeting was that said contracts as outlined were satisfactory, and on motion of Mr. Layng, seconded by Col. Smith, it was unanimously,

Resolved, that the question of entering into contracts relative to said reorganization be submitted to the Stockholders for consideration, and that favorable action by the Stockholders be and hereby is recommended.

Extract From Minutes of Meeting of Board of Directors of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, October 30, 1889 (R. 23; Ex. 23)

Resolved, that the officers of the Company be and they are hereby authorized to execute and deliver on behalf of this Company, the proposed contract with the Reorganization Committee of the Ohio, Indiana and Western Railway Company, substantially in the form now submitted, and also to execute and deliver on behalf of this Company, the proposed form of letter to said Committee relating to matters pending the reorganization, the officers being given full discretion to make any incidental changes in said contract or said letter which they deem expedient for the objects thereof, and in general to take all such steps as they may find expedient to give full and immediate effect to said objects,

Agreements made this 30th day of October, 1889 by and between The Cleveland, Cincinnati, Chicago and St. Louis Railway Company (hereinafter called the Cleveland Co.) and C. H. Coster, Samuel Spencer, George T. Bliss and Anthony J. Thomas, the Committee for Reorganization of the Ohio Indiana and Western Railway Company (hereinafter called the Committee),

Whereas the Committee is about to attempt the reorganization of the Ohio, Indiana and Western Railway Company substantially upon the basis set forth in the plan and agreement of reorganization hereunto annexed and made part of this contract; and

Whereas it is in contemplation to separate the lines of railway of said Company into the Western line, comprising the part from Indianapolis westward, and the Eastern line

comprising the part from Indianapolis eastward, substantially as the said lines formerly existed;

Now, therefore, these presents witness, that the said Cleveland Company covenants and agrees that when the Committee shall have so far carried out the said reorganization as that the said Western line and the said Eastern line shall have become or can be separated, then upon transfer and delivery to it of one half of the stock of the Company owning said Western line, issued under said reorganization, it will purchase or otherwise take over the said Eastern line, subject to and charged with a purchase money lien on the property only, amounting to $5,000,000 payable in one hundred years, with interest thereon in the meantime at 4 per cent per annum, payable annually out of income alone and non-cumulative, the said Western and Eastern lines being now subject to the lien of prior bonds for $500,000, it is understood that said prior bonds or bonds having an equal lien issued in place thereof as provided in the reorganization agreement shall have the benefit of said purchase money lien, the said purchase money lien shall be transferred by the Committee to the Company owning said Western line (and hereinafter called the Western Company) as security for the principal and interest of the new bonds to be issued under said plan of reorganization the interest on said purchase money lien to be applied in payment of the interest on the said prior bonds and the new First Consolidated Mortgage Bonds to be issued under said plan, The Cleveland Company will also simultaneously enter into a lease or other operating contract whereby it shall undertake the operation and management of said Western line, and agree

First, That the net earnings of said Western line shall be applied likewise to the payment of the interest to accrue on the said prior bonds, also on $1,000,000 other prior bonds having a lien on the Western line only and on said new First Consolidated Mortgage Bonds, and

Second, That the balance of such net earnings from the Western line and income derived from the lien on the Eastern line shall after payment of said interest be paid over to the Western Company, said lease or contract shall also contain covenants that the Cleveland Company shall provide for the due and punctual payment as it accrues of the interest on the said $1,500,000 prior bonds and on all said new First Consolidated Mortgage Bonds which may at any time be outstanding, and shall guarantee that the net earnings and income of the Western Company derived from both said lines shall not be less than $412,200 a year to be increased by the sum of $40 a year for each and every of said First Consolidated Mortgage Bonds issued in excess of $9,430,000 of said bonds as provided in said plan of reorganization and that the Cleveland Company shall look only to future surplus, net earnings and income of the Western Company derived from both said lines for its reimbursements of any sums advanced to make good any deficiency in said net earnings and income, with interest at six per cent per annum.

The said lease or contract of the Western line shall be for a term of years at the election of the Cleveland Company, but not less than 50 years and shall be assignable in whole or in part as additional security for the said First Consolidated Mortgage Bonds, and shall also contain covenants whereby said Cleveland Company shall undertake to

maintain said Western line and the rolling stock necessary for the operation of said Western line and pay all taxes thereon or upon the earnings or income of said Western line as well as rentals or other like charges, and to indemnify and save harmless said Western Company from all claims arising out of the operation or management thereof and also such other covenants, terms and conditions as may be reasonably required by said committee pursuant to the plan of reorganization or for the more perfect protection of the holders of said prior bonds and said new First Consolidated Mortgage Bonds and the new income bonds and stock to be issued under said plan of reorganization and the rights and interests intended to be granted to them.

It is further covenanted and agreed, that in the event that by reason of any legal impediment this agreement can not be carried out in its exact terms, a substantial compliance therewith may be required by either party from the other.

Extract From Minutes of Meeting of Board of Directors of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, February 25, 1890 (R. 23; Ex. 24)

The President stated to the Board, that at a meeting of the stockholders held October 30th, 1889 a resolution was passed authorizing the Board to make any contract or contracts providing for the acquisition of the line of railroad of the O. I. and W. Ry. Co. or any part thereof, either by purchase, lease, traffic contract or otherwise, as in their judgment may be best for the interests of this Company provided, however, that the fixed charges of this Company shall not be increased thereby by a greater sum than $435,000 per annum, in addition to such rentals as the O. I. and W. Ry. Company may pay for use of terminals or other property.

He further stated that the Reorganization Committee of the Ohio, Indiana and Western Railway Company had so far carried out said reorganization as that the Western line (i.e. from Indianapolis west) and Eastern line (i.e. from Indianapolis east) of said Company had been separated, pursuant to the terms of this Company agreement with them and that said Committee was ready to deliver to this Company one half of the stock of the Company owning said Western line.

He then submitted deed from the purchasers at foreclosure sale to this Company of the Eastern line subject to a lien of $5,000,000 declared and reserved thereon, and a copy of a deed transferring said purchase money lien to the Peoria and Eastern Railway Company.

Also copy of a deed from said purchasers to the Peoria and Eastern Railway Company conveying the fee of the part of the Western line situated in Illinois and perpetually leasing to said Company the part of said Western line situated in Indiana and all the rolling stock, late of the Ohio, Indiana and Western Railway Company.

Also an agreement between this Company and the Peoria and Eastern Railway Company, and copies of the two mortgages of the P. and E. Ry. Co. referred to in said agreement.

He stated that the general result of all these papers was that this Company acquires the ownership or is granted the lease or right to operate all the railway and property formerly of the O. I. and W. Ry. Co. at a net rental of $412,200 to be increased as in said agreements provided by $40 for each $1,000 First Mortgage Bonds of the Peoria Company issued in excess of $9,430,000.

These papers were then examined and discussed and

On motion of Mr. Twombley, seconded by Mr. Broadwell, it was unanimously resolved by the votes of all present that the officers of this Company be and they hereby are authorized and directed to execute and acknowledge in the name and on behalf of this Company and under its corporate seal the deed and agreement above mentioned, which reads as

(Copy of deed attached)

On motion of Mr. Townsend, seconded by Mr. McDonald, it was

Resolved by a like vote that the other papers presented at this meeting form part of their minutes by being annexed thereto, reading as follows

(Copy of documents attached)

And it was then further resolved by a like vote that the officers of this Company be and they hereby are authorized and directed to execute and acknowledge in like manner and on the demand of the Trustees of the First Consolidated Mortgage of the Peoria and Eastern Railway Company the independent covenants and agreements provided for in the second clause of the agreement between this Company and the Peoria and Eastern Railway Company.

And also that the officers of this Company be authorized generally to execute and acknowledge in like manner any and all other papers or instruments which may be deemed necessary or desirable effectively to carry out the purposes of the O. I. and W. Reorganization agreement on behalf of this Company pursuant to the agreement made October 30, 1889, between this Company and the Reorganization Committee of the O. I. and W. Ry. Co.

The President submitted to the Board, a form of letter addressed to Messrs. Coster, Spencer, Bliss and Thomas, Committee, as follows

Cincinnati, February 25, 1890

Messrs. C. H. Coster
Samuel Spencer
George T. Bliss Committee
A. J. Thomas

Dear Sirs:

Referring to the conveyance by Messrs. Coster and Spencer to this Company of the part of the line late of the Ohio, Indiana and Western Ry. Co. east of Indianapolis and to the lien of $5,000,000 declared and reserved by said grantors thereon, I beg to say that as part of the entire transaction this Company will enter into a satisfactory agreement whereby, in case of default, under either the first or second mortgage of the Peoria and Eastern Railway Company and of the proceedings thereunder against the mortgage premises said purchase money lien shall at once become due and enforceable, anything in said deed contained to the contrary notwithstanding but without personal liability on the part of this Company for the payment thereof as in said deed provided.

Yours very truly,

The Cleveland, Cincinnati, Chicago and St. Louis Railway Co.,
By M. E. Ingalls,
President.

Whereupon, on motion of Mr. Layng seconded by Mr. Brown, it was

Resolved, that the same be approved and the President authorized to sign and deliver to said Committee.

Extract from Minutes of Annual Meeting of Stockholders of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, October 30, 1889 (R.23; Ex. 25)

THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY STOCKHOLDERS ANNUAL MEETING, OCTOBER 30, 1889

The subject of a contract between this Company and the Committee for the Reorganization of the Ohio, Indiana and Western Railway Company having been submitted to this meeting

Resolved, by the unanimous vote of all Stockholders present in person or by proxy the holders of 138,203 shares of the Common Stock and 80,695 shares of the Preferred Stock of this Company voting in favor thereof

That the Board of Directors of this Company be and they hereby are authorized and empowered to make any contract or contracts providing for the acquisition of the line of railroad of the said O. I. and W. Ry. Co. or any part thereof either by purchase, lease, traffic contract, or otherwise as in their judgment may be best for the interests of this Company, provided however that the fixed charges of this Company shall not be increased thereby by a greater sum than $435,000.00, Four Hundred and thirty-five thousand dollars per annum in addition to such rentals as the O. I. and W. Ry. Co. may pay for use of terminals or other property.

Resolved, that the Directors of the Company be authorized and empowered to do everything necessary to carry out the provisions of the foregoing resolution.

Praecipe (R. 40)

[SAME TITLE AS FINAL DECREE]

To the Clerk of the United States District Court:

Please prepare a transcript of the record in the above-entitled cause in the matter of the petition for certiorari to be filed in the United States Supreme Court by the Income Bondholders of The Peoria and Eastern Railway Company, including in said transcript in the order given below the following papers:

1. Plan of Adjustment presented to Interstate Commerce Commission under Chapter XV.

2. Transcript of Testimony before Interstate Commerce Commission on Plan of Adjustment.

3. Petition, filed March 29, 1940, by The Peoria and Eastern Railway Company for the approval of said Plan.

4. Transcript of Testimony before Special Court with respect to Plan.

5. Opinion of Special Court, dated July 8, 1940.

6. Findings of Fact and Conclusions of Special Court, dated July 23, 1940.

7. Decree of Special Court, dated July 23, 1940.

8. Petition of The Peoria and Eastern Railway Company, dated January 8, 1941, to amend Decree.

9. Opinion of Special Court, dated April 3, 1941.

10. Order of Special Court supplemental to Decree, dated April 9, 1941.

11. Petition, dated December 12, 1942, of Income Bondholders for restoration of §24 of Decree.

12. Answer of The Peoria and Eastern Railway Company to said petition.

13. Order of Special Court, dated March 23, 1943, denying said petition.

14. Petition, dated April 1, 1943, of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company, et al. for appointment of a Special Master.

15. Answer of the Income Bondholders' Committee, dated April 8, 1943.

16. Order of Special Court, dated May 21, 1943, appointing Special Master.

17. Petition, dated June 24, 1943, by The Peoria and Eastern Railway Company with respect to the retention of Frank W. H. Adams to represent it.

18. Affidavit of Charles S. Aronstam, dated June 30, 1943, in opposition.

19. Order of Special Court, dated July 2, 1943, on said petition and affidavit.

20. Transcript of Testimony before Special Master, pages 1 through 4012-A.

21. Bondholders' Exhibits before Special Master, Exhibits A through ZZZZ and A-5 through K-12.

Praecipe

22. Peoria and Eastern's Exhibits before Special Master, Exhibits P & E-1 through P & E-54.

23. Operating Companies' Exhibits before Special Master, Exhibits 1 through 226.

24. Objections to Accounts, dated February 14, 1945, of Income Bondholders of The Peoria and Eastern Railway Company.

25. Motion, dated February 26, 1945, of Operating Companies to strike said objections.

26. Special Master's interim report, dated April 17, 1945.

27. Stipulation of the parties, dated August 28, 1946.

28. Report of Special Master, dated April 28, 1947.

29. Objections, dated May 12, 1947, of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company et al. to Report of Special Master.

30. Objections, dated May 13, 1947, of The Peoria and Eastern Railway Company to Report of Special Master.

31. Objections, dated May 29, 1947, of the Income Bondholders to the Report of the Special Master.

32. Motion, dated June 2, 1947, of The Cleveland, Cincinnati, Chicago and St. Louis Railway Company.

33. Opinion of the Special Court, dated April 26, 1948, upon the objections to the Special Master's Report.

34. Petition for Reargument, dated May 28, 1948, of Income Bondholders.

35. Opinion of Special Court, filed June 4, 1948, denying Petition for Reargument.

36. Order of Special Court, dated May 31, 1948, denying Petition for Reargument.

37. Stipulation of parties, dated October 15, 1948.

38. Opinion of Special Court, dated November 16, 1948, on Final Decree.

39. Final Decree, dated November 16, 1948.

40. This Praecipe.

Dated: January 5, 1949.

(s) Charles S. Aronstam,
Attorney for the Income Bondholders
of The Peoria and Eastern Railway Company,
50 Broadway,
New York, N. Y.

(s) John M. Harlan,
Root, Ballantine, Harlan, Bushby & Palmer,
Associate Counsel,
31 Nassau Street,
New York, N. Y.

We agree that the foregoing shall constitute the record in the Supreme Court of the United States in the above mentioned proceedings.

(s) GERALD E. DWYER,
Attorney for The New York Central Railroad Company and the Cleveland, Cincinnati, Chicago & St. Louis Railway Company.

(s) F. W. H. ADAMS,
Attorney for the Peoria & Eastern Railway Company.

FILE COPY

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CHARLES ELMORE

IN THE

Supreme Court of the United States

October Term, 1948

No. 511

IN THE MATTER OF
THE PEORIA AND EASTERN RAILWAY COMPANY

INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY,

Petitioners.

v.

THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

REPLY BRIEF OF THE PETITIONERS, INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY

CHARLES S. ARONSTAM,
ARTHUR A. BALLANTINE,
JOHN M. HARLAN,
Counsel for Petitioners.

ARCHIE S. KARP,
LYMAN M. TONDEL, JR.,
EDWARD L. FRIEDMAN, JR.,
WILLIAM B. SHEDD,
Of Counsel.

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IN THE

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REPLY BRIEF OF THE PETITIONERS, INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY

1. Jurisdiction

The respondents, the New York Central and Big Four, argue that petitioners are not proper persons to apply for certiorari. Section 745 of the Bankruptcy Act, 53 Stat. 1141 (1939) (set out in the Petition, p. 72), allows the appli-

cation by "any person affected by the plan." These respondents argue that under §706, petitioners are not "affected by the plan."

Section 706 provides:

> "Sec. 706. No creditor shall be deemed to be 'affected' by any plan unless such plan proposes a modification of the evidence of debt or other instrument defining the rights of such creditor, or a modification of the security, if any, for the claim of such creditor."

While petitioners, as will be seen below, pages 3-4, meet this test set up by §706, that section does not apply where, as here, the petitioners are asserting not their own rights as "creditors" but, in a derivative capacity, the rights of the Debtor, the Peoria and Eastern.

The present dispute is wholly one between the Debtor, the Peoria and Eastern, and the Operating Companies (see petition, p. 36). It involves the fiduciary standards to be applied as between them, and the determination of the inter-company accounts in accordance with those standards. The plan of adjustment, as now amended by the District Court to allow most of the claims of the Operating Companies, substantially resolves the issues against the Peoria and Eastern as a whole.

If the Peoria and Eastern were not dominated by the Operating Companies, it could without question have filed a petition for certiorari in its own interest. There can also be no question under §745 but that minority stockholders could petition in a derivative capacity on behalf of the Peoria and Eastern. If, because of §706, which applies only to "creditors", the Income Bondholders, whose derivative interest for this purpose is precisely

identical with that of the stockholders,* could not petition for certiorari in behalf of the Peoria and Eastern, the result would be at least anomalous, and probably unconstitutional. It is apparent, therefore, that §706 was not intended to, and does not, apply in connection with §745 when a creditor acts only in a derivative capacity to assert rights of the Debtor.

Moreover, we have shown in the Petition, pp. 19-20, that in every practical sense the Income Bondholders, themselves, have a direct and vital interest in the plan of adjustment as *now* amended by the District Court, and that they are thus affected by it. (The contrary finding, referred to at p. 7 of the brief of the New York Central and Big Four, was made *before* the modifications of the plan now in question, and is therefore irrelevant here.)

The effect of the plan on petitioners comes within the language and meaning of §706. The "instrument defining the rights" of the petitioners is the Income Mortgage, which is by its terms subordinate in certain respects to the Operating Agreement (S. 185). The Plan makes determinations with respect to the fiduciary standards under the Operating Agreement and with respect to the alleged operating debt. These determinations clearly affect the "security" for the income bonds. See *Matter of Kinney*, 279 N. Y. 423, 431-432, 18 N. E. (2d) 645, 649 (1939); noted in 39 Columbia Law Rev. 1037 (1939). Indeed the plan as now amended by the District Court would not only impair the value of the Income Bonds, but for all practical

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* At an earlier stage of this proceeding, the District Court said that the "income bondholders occupy much the same position as preferred shareholders, and as such they have a very lively interest in the payment of the accumulated advances." *Ewen* v. *Peoria & E. Ry. Co.*, 34 F. Supp. 332, 338 (S. D. N. Y., 1940).

purposes would remove all restraints on the Operating Companies' "use" of the Peoria and Eastern.

2. The Inter-company Accounts.

The respondents, the New York Central and the Big Four, make two points as to the inter-company accounts, pp. 5-6, first, that they accurately set forth the "actual receipts and disbursements" of the Peoria and Eastern, and, second, that they were kept in conformity with Interstate Commerce Commission requirements.

As stated in the petition, pp. 10, 11, 15 and 22, the inter-company accounts set forth *only* what the Operating Companies, themselves, as a part of their self-dealing apportionment of joint revenues and expenses, had determined should be the "actual" receipts and disbursements of the Peoria and Eastern.

The Interstate Commerce Commission Uniform System of Accounts, as the name implies, is concerned with the method of setting up the books of a company, with a view towards promoting uniformity of railroad accounts. It has no bearing upon the self-dealing methods employed by the Operating Companies to determine the Peoria and Eastern's revenues and expenses. The comptroller of the Operating Companies so testified. See R. 20, pp. 2472-2473. Indeed the District Court held that the Commission lacked jurisdiction over these questions. See Petition, p. 41, and S. 31.

3. The Standard of Fiduciary Duty.

It will be noted that the respondents, the New York Central and the Big Four, make no attempt to justify, and indeed do not even mention, the indefensible fiduciary

standards laid down by the District Court, including the erroneous placing of the burden of proof on the beneficiary. Nor do these respondents suggest any other standard; they go no further than to argue that the usual fiduciary standards do not apply (Brief, pp. 8-13). They cite nothing in the Operating Agreement specifically warranting any relaxation of the rules as to a self-dealing fiduciary; there is only a quotation of the District Court's statement as to what the Agreement "presupposed".

These respondents appear to argue also (p. 11) that the rule of *Pepper* v. *Litton*, 308 U. S. 295 (1939), to the effect that the burden of proof is on the fiduciary to show fairness in his self-dealing transactions, applies only in cases of "spoliation, mismanagement and faithless stewardship." The fiduciary standards, of course, apply regardless of spoliation. *Southern Pacific Co.* v. *Bogert*, 250 U. S. 483, 492 (1919). If the fiduciary duties are not satisfied, the fiduciary's claim is disallowed or the fiduciary is surcharged. Similarly, respondents' quotation of the District Court's statement that they had acquitted themselves creditably in the inter-company transactions, is beside the point. This statement, of course, means only that the Operating Companies did not violate the District Court's standards, which, in their practical application, placed no restrictions upon them.

4. The Items of Account.

The respondents, the New York Central and the Big Four, erroneously assert that the petitioners in their discussion of the items of account, petition, pp. 40-55, are merely seeking to review facts concurrently found by the Special Master and the District Court (Brief, p. 15). This misses the entire point of this portion of the petition, the

purpose of which was to show that the result in each instance depended upon the erroneous fiduciary standards (which are standards of law) laid down by the District Court (see Petition, pp. 40-55).

5. The Brief of the Peoria and Eastern.

The position of counsel, selected for the Peoria and Eastern by its adversaries, the Operating Companies (see Petition, p. 14), is characteristic of what has happened at all stages of this litigation. As we pointed out in the petition, p. 14, he has throughout the case opposed all the major positions advocated by the Income Bondholders in behalf of the Peoria and Eastern. In this instance, while his brief is merely submitted "with respect to the petition," its tenor is one of opposition to review by this Court. The brief even goes beyond the District Court's holding of limited fiduciary duties, and the recognition by the Operating Companies of "modified" fiduciary duties (brief of N. Y. Central, pp. 9-10), to assert that the "relationship of the parties . . . does not involve any fiduciary duty . . ." (brief of P. & E., p. 16).

The fact is that here, as throughout this proceeding, the real interests of the Peoria and Eastern have been represented by the Income Bondholders (see pp. 2-3, *supra*), rather than by counsel for the Peoria and Eastern.*

---

* Counsel also refers (p. 18) to the fact that the Peoria and Eastern "was deprived of interest" on its earnings for the years 1942-1944, held by the New York Central pending the disposition of this case (S. 77-78). It should be noted that counsel for the Peoria and Eastern, after stating to the District Court that he had recognized the question from the beginning of his participation in the case but took no action upon it, opposed the allowance of such interest to his client.

6. Conclusion.

This case, as shown in the petition, involves far more than the interpretation of the Operating Agreement or determination of issues of fact, as stated by the respondents, the New York Central and the Big Four, brief, p. 16. If the District Court was right, then the fiduciary standards laid down in this Court's opinions would be worthless as a protection against excesses of fiduciaries, in any case where the fiduciary takes the precaution of patterning its relationships with its beneficiary upon those presented here.

We submit that these questions are of such far-reaching importance as to deserve this Court's attention.

Respectfully submitted,

CHARLES S. ARONSTAM,
ARTHUR A. BALLANTINE,
JOHN M. HARLAN,
Counsel for Petitioners.

ARCHIE S. KARP,
LYMAN M. TONDEL, JR.,
EDWARD L. FRIEDMAN, JR.,
WILLIAM B. SHEDD,
Of Counsel.

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IN THE

Supreme Court of the United States

October Term, 1948

No. 511

IN THE MATTER OF

THE PEORIA AND EASTERN RAILWAY COMPANY

INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY,

Petitioners,

v.

THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

MOTION TO DISPENSE WITH THE PRINTING OF THE RECORD AS REQUIRED UNDER RULE 38, PARAGRAPHS 1 AND 7, ON CONSIDERATION OF THE PETITION FOR A WRIT OF CERTIORARI

CHARLES S. ARONSTAM,
ARTHUR A. BALLANTINE,
JOHN M. HARLAN,
Counsel for Petitioners.

IN THE

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MOTION TO DISPENSE WITH THE PRINTING OF THE RECORD AS REQUIRED UNDER RULE 38, PARAGRAPHS 1 AND 7, ON CONSIDERATION OF THE PETITION FOR A WRIT OF CERTIORARI

Petitioners have filed with this Court a petition for a writ of certiorari to the United States District Court for the Southern District of New York, pursuant to §745 of the Bankruptcy Act, as enacted in 53 Stat. 1134 (1939), to re-

view the final decree of that Court, entered November 16, 1948, in the Railroad Adjustment Proceeding entitled In the Matter of The Peoria and Eastern Railway Company.

The transcript of record certified to this Court is extremely voluminous. It was not printed upon the review of the Special Master's Report in the Special District Court. It consists of over 4,000 typewritten pages of testimony and over 550 exhibits (which, it is estimated, contain well over 30,000 pages), as well as opinions, orders, petitions, answers, and other court papers.

Most of this material is unnecessary to the consideration of the petition for the writ. Those portions of the record which petitioners deem necessary to consideration of the questions presented have been printed as an exhibit to the petition, separately bound, and called Supplement I; in addition, ten copies of the report of the Special Master are being furnished for the use of this Court.

WHEREFORE, petitioners pray for an order dispensing with the printing of the certified transcript of record in this case in connection with the consideration of the petition for a writ of certiorari filed by petitioners.

CHARLES S. ARONSTAM,
ARTHUR A. BALLANTINE,
JOHN M. HARLAN,
Counsel for Petitioners.

FEB 11 1949
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

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THE PEORIA AND EASTERN RAILWAY COMPANY.

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THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

BRIEF OF RESPONDENTS, THE NEW YORK CENTRAL RAILROAD COMPANY AND THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

GERALD E. DWYER,
Counsel for Respondents, The New York Central Railroad Company and The Cleveland, Cincinnati, Chicago and St. Louis Railway Company.

SAMUEL H. HELLENBRAND,
LEE P. GAGLIARDI,
Of Counsel.

THE COURT PRESS, N. Y. C.

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BRIEF OF RESPONDENTS, THE NEW YORK CENTRAL RAILROAD COMPANY AND THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUS RAILWAY COMPANY IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Statement.

Petitioners, Income Bondholders of The Peoria and Eastern Railway Company, seek a writ of certiorari to review a final decree of the United States District Court for the Southern District of New York, settling and stating as of December 31, 1945, the intercompany accounts between the Peoria and Eastern and the Operating Companies.* The decree was

---

* The parties will be referred to herein as follows:
Peoria and Eastern—The Peoria and Eastern Railway Company
New York Central—The New York Central Railroad Company
Big Four—The Cleveland, Cincinnati, Chicago and St. Louis Railway Company
Operating Companies—New York Central and Big Four

entered upon the unanimous decision (*Ewen, et al.* v. *Peoria and Eastern Railway Co.*, 78 F. Supp. 312) of a three-judge Special Court consisting of Chief Circuit Judge Learned Hand and District Judges Coxe and Hincks, substantially confirming the report of a special master made after extended hearings which involved some 4000 pages of testimony and 577 voluminous exhibits.

The proceeding before the Special Master arose out of and is supplemental to a railroad adjustment proceeding brought by the Peoria and Eastern under the provisions of former Chapter XV of the Bankruptcy Act (53 Stat. 1134).* By decree entered July 8, 1940 (*Ewen, et al.* v. *Peoria and Eastern Railway Co.*, 34 F. Supp. 332, cert. denied 311 U. S. 700), and order supplemental to decree dated April 29, 1941 (*In re Peoria and Eastern Railway Company*, 37 F. Supp. 917, cert. denied 314 U. S. 635), the Special Court granted the petition of the Peoria and Eastern for adjustment of its maturing bond indebtedness, but made no adjudication with respect to the amount and validity of the accounts between the Peoria and Eastern and the Operating Companies, leaving all questions concerning them open and reserved for future determination. In April, 1943, the Special Court granted the petition of the Operating Companies for the appointment of a special master to hear and report on the amount and validity of the inter-company accounts.

From the beginning of its corporate existence in 1890 the railroad of the Peoria and Eastern has been operated by the Big Four (and, subsequent to 1930, by the New York Central under its lease of the Big

* Printed as Appendix to petition for certiorari.

Four) under the provisions of an Operating Agreement (Ex. 11, S. 160)* entered into in 1890 between the Big Four and the reorganization committee of the insolvent predecessor of the Peoria and Eastern.

This Operating Agreement was part of a comprehensive plan of reorganization adopted by the reorganization committee and security holders of the insolvent company (Ex. 3, S. 156—in part—). The salient features of this plan (the third foreclosure and reorganization of the same line of railroad within a ten year period) included the sale to the Big Four of the easterly segment of the railroad running from Indianapolis, Indiana to Springfield, Ohio; the conveyance to the newly incorporated Peoria and Eastern of the westerly segment of the road running from Indianapolis, Indiana to Pekin, Illinois; the issue by the Peoria and Eastern of First Mortgage 4% bonds, Second Mortgage non-cumulative 4% Income Bonds and capital stock to be exchanged for various securities of the predecessor company; a guarantee by the Big Four of payment of the interest on the Peoria and Eastern first mortgage bonds and the prior bonds of the predecessor companies of the Peoria and Eastern; and the delivery to the Big Four of half the authorized capital stock of the Peoria and Eastern as consideration for its entering into an agreement for the operation of the railroad of the Peoria and Eastern (Findings 5-9, 13, S. 108; Exs. 3-9, 11, S. 160).

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* Since petitioners are moving to dispense with the printing of the record and have printed only a few selected documents as Supplement 1 to their petition, our references to matters printed therein will be designated "S. . . ."; where we refer to matters not printed in Supplement 1 our references will be to exhibits and typewritten minutes in the record before the Special Master. References to the report of the Special Master will be made as "S. M. . . .".

The plan of reorganization was consummated by the execution of the necessary documents on February 22, 1890 (Exs. 5, 10, 11, 13, S. 178) and the Big Four thereupon commenced its operation of the railroad of the Peoria and Eastern.

The Operating Agreement (Ex. 11, S. 162) recites:

> "WHEREAS the railways of the parties hereto connect at Indianapolis, and it will be beneficial to the business and traffic of said railways that the same be put under one management:"

and provides that the Big Four "contracts and arranges with the Peoria Co. for running the railroad of the Peoria Co."; the Peoria and Eastern grants to the Big Four "the right to use and operate" its railroad and the Big Four agrees that it will "use, maintain and operate" the railroad (Article First). The Big Four agrees to make all necessary expenditures (Article First) and to make good any deficiency required for the payment of interest on the first consolidated mortgage bonds of the Peoria and Eastern and on the prior mortgage bonds (Article Second). While the agreement provides that the Big Four is to receive all earnings and income of the use and operation of the railroad, it is required to apply such receipts to the expenses of operation and payment of interest and, if any surplus remains, it is required to be paid to the Peoria and Eastern (Article Third). The agreement (Article Fourth) also requires the Big Four annually to make up and state all its receipts and disbursements and "to render proper accounts therof to the Peoria Co. and to the trustees of its said second mortgage as in said second mortgage required."

During the 50 years between the execution of the Operating Agreement and the commencement of the adjustment proceeding the Big Four and its lessee, the New York Central, operated the railroad of the Peoria and Eastern, making all necessary expenditures required for its maintenance, operation and improvement, crediting the Peoria and Eastern with all receipts from operation and making good any deficiencies required for the payment of interest on the first mortgage bonds and prior mortgage bonds. Annual accounts were filed with the Board of Directors of the Peoria and Eastern and with the trustees of the Income Mortgage, as required by the Operating Agreement and the Income Mortgage (Ex. 13, S. 178), and annual statements were furnished to stockholders.

At the hearings before the Special Master the Operating Companies offered in evidence their accounts for those years to which the director representing the Income Bondholders had objected, and also offered, as accounts stated, their accounts for each of the years back to 1926, accompanied by testimony that all of these accounts were kept in conformity with the regulations and requirements of the Interstate Commerce Commission and correctly set forth the amounts received and expended by the Operating Companies on behalf of the Peoria and Eastern. The Operating Companies also proved that the accounts had been duly rendered each year to the Peoria Company and to the Trustees of the Income Mortgage in accordance with the requirements of the Operating Agreement and of the Income Mortgage (R. 153-240).

At no time did the Income Bondholders or the accountants retained by them to investigate the accounts challenge the fact that the accounts as received in evidence accurately set forth the actual receipts

and disbursements of the Peoria and Eastern. Instead, the Bondholders undertook to prove that the accounts should be revised in large amounts in favor of the Peoria and Eastern by the application of methods and practices contended for by their witnesses upon the theory that the Operating Companies were required to operate their entire railroad system for the sole benefit of the Peoria and Eastern. The Operating Companies produced witnesses whose testimony demonstrated that the methods and practices which had been followed for more than 50 years were fair to both parties.

The claims asserted by the petitioners against the Operating Companies totaled millions of dollars. The findings of the Special Master on these claims, as slightly modified by the Special Court, allowed claims in the principal amount of approximately $130,000 and rejected the balance.

Jurisdiction of This Court.

Before discussing the merits of the pending application for certiorari, we beg leave to refer to the statutory provision upon which the petitioners base their claim of the Court's jurisdiction (Petition p. 19).

Article XV of the Bankruptcy Act, which was approved July 28, 1939 and expired by its own terms on July 31, 1940, provided a simple and inexpensive method for railroads which were solvent, but temporarily unable to meet maturing debts, to adjust such debts. The law authorized the approval of a plan of adjustment by a three-judge Special Court and specified the parties entitled to appeal and the method

by which appeal might be taken. Section 745 of the statute, upon which petitioners rely, provides:

> "Any final order or decree of the special court may be reviewed by the Supreme Court of the United States upon application for certiorari made by any person affected by the plan who deems himself aggrieved * * * "

Petitioners argue that they are "clearly aggrieved by this portion of the Plan" but wholly ignore Section 706 of the Act, the terms of which preclude an application by petitioners. That section provides:

> "No creditor shall be deemed to be 'affected' by any plan unless such plan proposes a modification of the evidence of debt or other instrument defining the rights of such creditor, or a modification of the security, if any, for the claim of such creditor."

The decree appealed from neither "proposes a modification of the evidence of debt or other instrument defining the rights" of the petitioners "or a modification of the security, if any", for the claim of petitioners.

The adjudication in the 1940 adjustment proceeding included a finding that the only claims affected by the Plan were the First Consolidated Bonds; the petitioners were authorized to intervene as persons in interest under Section 720, not as parties affected by the Plan. (*Ewen, et al.* v. *Peoria and Eastern Railway Co.*, 34 F. Supp. 332, cert. denied 311 U. S. 700; *In re Peoria and Eastern Railway Company,* 37 F. Supp. 917, cert. denied 314 U. S. 635.)

Issues Before This Court.

The question of jurisdiction to one side, the only real issue presented on this application is petitioners' contention that the decision sought to be reviewed is in conflict with decisions of this Court defining standards of duty imposed on certain fiduciaries and the corollary burden of proof resting on such fiduciaries.

Petitioners also assert error in the decision of the Special Court holding their claims barred by the doctrine of accounts stated and by the statute of limitations, and discuss the merits of some of their specific claims which were rejected by the findings of the Special Master as confirmed by the Special Court.

Duty of the Operating Companies and Burden of Proof.

In none of the cases relied upon by the petitioners (*Pepper* v. *Litton,* 308 U. S. 295; *Taylor* v. *Standard Gas & Electric Co.,* 306 U. S. 307; *Southern Pacific Co.* v. *Bogert,* 250 U. S. 483; *Geddes* v. *Anaconda Mining Co.,* 254 U. S. 590, and others) was the management and stock control of the subsidiary company conferred upon the controlling company by the voluntary agreement of the security holders of the subsidiary company, as part of a transaction which included a contract for the joint operation of the business of both companies for their mutual benefit by the management of the controlling company.

The major error in the petitioners' contentions is the fallacious premise that the written instrument creating the relationship, and the circumstances surrounding its execution, are of no significance in de-

fining the rights and responsibilities of the parties, and that the mere existence of a fiduciary relationship completely delineates and defines such duties and rights without regard to contractual relationships established at arms-length.

In *Securities Commission* v. *Chenery Corp.*, 318 U. S. 80, this Court said, pages 85, 86:

> "But to say that a man is a fiduciary only begins analysis; it gives direction to further inquiry. To whom is he a fiduciary? What obligation does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?"

In support of their theory petitioners emphasize the Big Four's ownership of a majority stock interest but disregard the effect of the contract between the parties and the circumstances under which the Operating Companies acquired their majority stock interest.

In 1889 the predecessors of the present Income Bondholders had upon their hands a railroad venture which had been consistently unsuccessful and was subject to mortgage liens in a large amount (Finding 5). They formulated a plan of reorganization which depended for its success upon inducing the Big Four to undertake the operation of their railroad, and the Operating Agreement and other documents were executed. The security holders of the Peoria and Eastern agreed and intended that the Big Four should receive a controlling stock interest in the new company as an inducement to undertaking its operation (Exs. 3, 21); they knew and agreed that there would be a unified management and joint operation of the railroads of both companies; they knew and agreed that

the Operating Agreement contemplated and required benefit to both roads. The Operating Agreement expressly so recites (Ex. 11, S. 162).

On these undisputed facts both the Special Master and the Special Court held that the conventional fiduciary duties which might have arisen out of the mere fact of control were modified by agreement of the parties as shown by the terms of their contracts considered in the light of their respective situations at the time of making the contracts. The Special Court said (*Ewen, et al.* v. *Peoria and Eastern Railway Co., supra,* page 316):

> "We shall assume that, as its majority shareholder, the 'Central' would have been subject to the usual limitations of a trustee in any dealings between the two, had it not been for the powers granted it in the 'Agreement'; but both the Bondholders and the 'Peoria' concede that these to some extent modified its duty. A moment's reflection shows that if it were to be held strictly accountable as a fiduciary in the conventional sense, the 'Agreement' could not have been performed at all. Both parties entered into it, because, as it recites, they thought that it would be 'beneficial to the business and traffic of said railways that the same be put under one management'; and 'one management' presupposed that the 'Central' should have power to determine the interests of both in those mutual transactions which would constantly arise between the two. Moreover, it was apparent that those determinations could not be 'beneficial' at once to the 'business and traffic' of the 'Central' and of the 'Peoria,' unless the 'Central' were permitted to

> profit from the joint 'business and traffic.' Indeed there would have been no conceivable motive for its entering into the agreement at all, if it were bound to fix the terms of every transaction with an eye only to the interest of the 'Peoria.' "

Even if the agreement between the majority and minority interests in this case did not distinguish it from the decisions cited by petitioners there would still be no conflict between the conclusions of the Special Court and the principles laid down by this Court.

The limitation on the broadly stated doctrines of fiduciary duty and burden of proof in the cited cases has been recognized by this Court in the recent case of *Comstock* v. *Group of Institutional Investors,* 335 U. S. 211, 228, 237. There both the majority and the minority quoted the statement in *Pepper* v. *Litton, supra,* pointing out that the doctrine in the *Taylor* case was based on "the equities of the case—the history of spoliation, mismanagement, and faithless stewardship of the affairs of the subsidiary." Here the Special Master found that "there has been no evidence of fraud or of calculated overreaching in the entire case" (S. M. 287), and the Special Court found "no justification for saying that it [New York Central] ever deliberately tried to despoil the 'Peoria'; or that the matters with which we do charge it show evidence of any corrupt purpose. * * * on the whole, it acquitted itself creditably in a long series of extremely complicated transactions." (*Ewen, et al.* v. *Peoria and Eastern Railway Co., supra,* 326.)

The proof in this case also follows the pattern of proof in the *Comstock* case, as quoted and approved by this Court (pp. 221, 222, 225):

> "The expert accountant called by Comstock produced a large number of exhibits which he

had prepared from the books, records and reports of the individual companies and explained in connection with them the inferences he had drawn from his studies and expressed his opinions tending to support the Comstock charges. * * *

"The Group of Institutional Investors * * * to sustain the burden of Missouri Pacific defense called as their witnesses on the trial the railroad men who had engaged, each in his own department, in all of the transactions and railroad operations and the records made thereof throughout the period involved, and they testified of and concerning matters with which they were intimately familiar. * * *

"* * * But the disputes and conflicts of testimony in respect to the accounts and the inferences to be drawn were all issues of fact. * * *

"Comstock's contention that the court erroneously put the burden of proving his charges on him rather than requiring the Missouri Pacific to proceed first to disprove them, is without merit. As the execution of the promissory notes was admitted and at least formal proof of all of the items of advancements making up the debt had been in the record of the Section 77 proceedings for many years before the hearing, the court required only that all the records of the transactions that were questioned be made available for the hearing so that there was the equivalent of a full disclosure by the Missouri Pacific before Comstock was required to proceed with his proof of the charges. In its findings the court stated the facts as it found them to be proven by the whole evidence."

In the present case formal proof of the accounts was made and all the basic records were made available to petitioners' accountants who spent more than a year in investigating them. The testimony offered by petitioners' witnesses consisted principally of tabulations taken from the Operating Companies' records accompanied by the opinions of these witnesses that the various charges and credits should have been made upon bases suggested by them. The respondents then offered the testimony of railroad operating officers explaining the bases upon which the charges and credits were made and demonstrating the fairness of the transactions to both parties. Upon the whole evidence the Special Master's findings of fact dismissing the bulk of the claims asserted were confirmed by the Special Court.

Accounts Stated.

The subsidiary question raised by petitioners with respect to accounts stated is unimportant to the consideration of this petition, since the doctrine of accounts stated was not actually applied to their claims.

The contention of petitioners is in reality a complaint against the agreements made by their predecessors more than fifty years ago. The Operating Agreement provides for an annual accounting. Each year the Big Four is required to "make up and state all its receipts for earnings and income * * * and for the cost and expense of using, operating and maintaining said lines of railroad * * * and to render proper accounts thereof to the Peoria Co. and to the trustees of its said second mortgage as in said second mortgage required" (S. 166).

The Income Bond Mortgage, which by its terms

is subordinate to the Operating Agreement (S. 185), requires the directors of the Peoria and Eastern to ascertain the net earnings of the Peoria and Eastern and to furnish the trustees annually with a statement showing such net earnings. Detailed procedure for objecting to the accounts and for settlement of disputes, and the exclusive remedy to be used in case of non-settlement, are prescribed by Article Sixth of the Income Mortgage (S. 193-195).

Upon the hearings the Operating Companies proved both by its own officers and by an officer of the Income Mortgage Trustee that the annual accounts had been duly filed year by year in accordance with the terms of the contracts. The claim of error in the holding with respect to accounts stated cannot be sustained without disregarding or voiding the provisions of the contracts, and no justification has been shown for doing so.

Statute of Limitations.

The claims actually asserted and litigated in this proceeding are claims of mismanagement, overreaching and breach of duty and the proceeding is, in substance, an equity proceeding.

The Operating Companies were required to file annual accounts of the result of their operations, and any interested security holder of the Peoria and Eastern could have advanced and litigated the claims now asserted at any time after the filing of each annual account. Accordingly, the Special Court properly held the equity ten year Statute of Limitations applicable to these claims. (New York Civil Practice Act, Sec. 53.)

The petitioners argue that the statute of limitations is inapplicable because the adjustment proceed-

ing, from which this proceeding stems, was brought under the provisions of the Bankruptcy Act, and cite *Holmberg* v. *Armbrecht,* 327 U. S. 392; *Guaranty Trust Co.* v. *York,* 326 U. S. 99; *Vanston Bondholders Protective Committee* v. *Green,* 329 U. S. 156. These cases do not support the view urged by the Bondholders. The *Holmberg* case deals with a federally created right under the Federal Farm and Loan Act; the *Guaranty Trust* case holds that where the rights are not federally created but are created under state law, as admittedly is the situation here, the applicable state statute of limitations does apply; and the problem in the *Vanston* case is whether a claim assumed valid under state law should be recognized under the Bankruptcy Law.

Specific Claims of Petitioners.

The report of the Special Master with respect to petitioners' specific claims, as confirmed by the Special Court, consists principally of findings of fact which "the seasoned and wise rule of this Court makes * * * final here in the absence of very exceptional showing of error." *Comstock* v. *Group of Investors, supra,* 214; *Anderson* v. *Mt. Clemens Pottery Co.,* 328 U. S. 680, 689.

The report of the Special Master demonstrates that these findings were made after full and careful consideration of conflicting and detailed evidence submitted by the respective parties on each of the claims involved, and "this Court does not grant certiorari to review evidence and discuss specific facts". *Wisconsin Electric Co.* v. *Dumore Co.,* 282 U. S. 813.

Conclusion.

The decision which this Court is asked to review involves the meaning and effect of contracts between the parties, and the determination of issues of fact resolved after consideration of voluminous conflicting evidence. "The asserted conflict in decisions arises from differences in states of fact, and not in the application of a principle of law." *United States* v. *Johnston,* 268 U. S. 220, 227, and the decision here is of interest to no one but the immediate parties.

We respectfully submit that no reasons have been shown which warrant review by this Court, and the petition for writ of certiorari should be denied.

Respectfully submitted,

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LEE P. GAGLIARDI,
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1948.

No. 511.

In the Matter of

THE PEORIA AND EASTERN RAILWAY COMPANY.

INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY,

Petitioners,

v.

THE NEW YORK CENTRAL RAILROAD COMPANY, THE CLEVELAND, CINCINNATI, CHICAGO AND ST. LOUIS RAILWAY COMPANY and THE PEORIA AND EASTERN RAILWAY COMPANY.

BRIEF OF THE PEORIA AND EASTERN RAILWAY COMPANY WITH RESPECT TO THE PETITION FOR WRIT OF CERTIORARI OF THE INCOME BONDHOLDERS OF THE PEORIA AND EASTERN RAILWAY COMPANY.

Foreword.

This proceeding was originally commenced in 1940 by the Peoria* pursuant to Chapter XV of the Bankruptcy Act (53 Stat. 1134) for approval of a Plan of Adjustment which had been approved by the Interstate Commerce Commission (239 I. C. C. 303).

* We have used the following abbrevations:

P. & E., or the Peoria—the respondent, The Peoria and Eastern Railway Company.

Big Four—the respondent, The Cleveland, Cincinnati, Chicago and St. Louis Railway Company.

[Footnote continued on following page.]

The adjustment was sought because in 1940 the First Mortgage Bonds of the Peoria were about to become due, and the operating agreement of 1890 between the Peoria and the Big Four was to expire (S. M. 6, 7).*

The District Court approved the Plan of Adjustment (R. 5-7). *Ewen* v. *Peoria and Eastern Railway Co.,* 34 F. Supp. 332. The plan, however, did not liquidate the operating deficit accumulated against the Peoria under the operating agreement or the reserve and depreciation accounts in its favor. The Court, therefore, left these questions open, providing that one director of the Peoria should represent the Income Bondholders, who had been permitted to intervene in the proceeding. Section 24 of the decree of the Special District Court, as amended in 1941, provides as follows:

> "All questions concerning the amount and validity of the accounts between the 'Big Four', the New York Central Railroad Company and the Petitioner are not determined in these proceedings and are hereby specifically left open and re-

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[Footnote continued from preceding page.]

New York Central—the respondent, The New York Central Railroad Company, controlling stockholder of the Big Four, and after 1930 lessee of its property, including its interest in the P. & E. (*infra,* p. 12).

Operating Companies—New York Central and Big Four.

Income Bondholders—petitioners, a Protective Committee of the P. & E.'s Second Mortgage non-cumulative 4% Income Bonds, due 1990.

* "S." references are to the material in Supplement I, and "S. M." references are to the Special Master's report, Supplement II. "R." references are to the unprinted record, and are keyed to the items listed in the Praecipe, which is printed at S. 213. The numeral following the letter R. refers to the item in the Praecipe bearing that number.

served for future determination. Should the New York Central Railroad Company and/or the 'Big Four' seek or attempt, in any year or at any time or times hereafter, to withdraw any part of the earnings or assets of the Petitioner by way of recoupment or repayment of said inter-company accounts, then and in such event said New York Central Railroad Company and/or 'Big Four', upon objection by the representatives of the Income Bondholders elected to the Board of Directors, must prove and establish their right to do so" (S. 154).

Early in 1943 the New York Central filed the annual account between the roads required by Article Fourth of the operating agreement, to which the director of the Peoria who had been appointed by the Income Bondholders filed objections. Thereafter, and on April 1, 1943, the New York Central petitioned for a supplemental order appointing a master under the decree to hear and report upon the validity and amount of their claim against the Peoria in the sum of $2,356,687.33, as of December 31, 1942 (S. 79-91); and by order entered May 21, 1943, the District Court appointed a master to conduct such an inquiry (S. 92-4). The parties to the accounting were the New York Central, a Protective Committee of the Income Mortgage Bondholders, and the Peoria.

On July 2, 1943, the Court appointed the undersigned, as an independent attorney to represent the Peoria, upon the petition of the New York Central, with the understanding that he should "to the best of his ability as an attorney, protect the interest of the Peoria and Eastern * * * and * * * look only to the best interest of the Peoria and Eastern without regard to any * * * control," by the New York Central (S. 96; 99; 12).

Thereafter, as such independent counsel, the undersigned considered the proposed accounts, investigated the records of both the Peoria and the operating companies, conferred with operating, accounting and other officials of the Peoria and the operating companies, considered the report prepared by accountants for the Income Bondholders and generally investigated all possible issues.

With respect to each issue, consideration was given not only the over-all interests of the Peoria in relation to past transactions, but also in relation to its future welfare, insofar as that welfare may be affected by this proceeding, without regard to the special interests of any particular group of security holders.

In endeavoring to protect the Peoria's entire interests we have not been unmindful of the fact that this road has been operated for fifty years, as a part of a system under the operating agreement, and that the District Court in its decree of July 29, 1940, approved an extension of that agreement for an additional twenty years.

Under these circumstances, the mere fact that the Income Bondholders saw fit to assert a particular claim did not, in our view, create an identity of interest between the P. & E. and the Income Bondholders, or provide a sufficient basis for adopting it. For the same reasons, where a claim of the Income Bondholders appeared to be detrimental to the best interests of the Peoria, or without merit, we have not hesitated to oppose it.

ARGUMENT.

I.

The Income Bondholders assert as their principal reason for the granting of certiorari that the District Court erred in failing to find that the Operating Companies are fiduciaries of the P. & E. and that as such fiduciaries the Operating Companies must be held to the fiduciary standards laid down by such decisions of this Court as *Pepper* v. *Litton,* 308 U. S. 295; *Schwabacher* v. *United States,* 334 U. S. 182; *Geddes* v. *Anaconda Mining Co.,* 254 U. S. 590; *Comstock* v. *Group of Investors,* 335 U. S. 211.

We believe this contention to be contrary to the facts upon which the relationship of the parties is based, contrary to the actual day to day construction and operation of the P. & E. under the operating agreement for over fifty years and not in the best interests of the P. & E., now or in the future.

We believe that the case involves only the construction of a special contract which was born of the mutual interests of the parties and which contemplated the operation of the P. & E. as part of a single system.

A determination of this basic question involves an examination of the history of the P. & E. prior to the commencement of this proceeding.

The immediate predecessor of the Peoria was the Ohio, Indiana and Western Railroad* which owned and operated a line from Peoria, Illinois to Springfield, Ohio. That road was apparently born of early insolvencies and, in its turn, reached that stage by 1888.

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* Sometimes referred to as the "O. W. & I."

Security holders, in a salvage effort, formed a Re-organization Committee known as the Coster Committee.

The Re-organization Plan proposed by this Committee, and the contract with the Big Four, which incorporated the plan into its terms (S. 156-159; Ex. 3, R. 23) is, in our view, of aid in understanding both the relationship of the parties and the legal principles which have governed them.

The plan indicates that the O. W. & I. was in danger of foreclosure and eventual liquidation and that the security holders, of various classes desired to protect their interests. It contemplated a separation of the O. W. & I. into two lines, to be operated separately, and independently. One part, known as the Eastern line or Springfield division, ran east of Indianapolis and was to be conveyed in fee to the Big Four. The Western line was to be conveyed to a corporation (now the P. & E.) to be formed by the Committee and to be operated under a "lease, contract or other arrangement" by the Big Four (S. 156-159; Ex. 3, R. 23).

The plan provided for the issuance of new securities, including the so-called Income Bonds in the amount of $4,000,000 and common stock in the amount of $10,000,000.

The plan itself shows clearly that it was contemplated that one-half of this stock would go to the then holders of common stock of the O. W. & I., at the rate of one share of new stock for two of the old, and that one-half of the new stock was "to be used under proposed arrangement with C. C. C. & St. L. Ry." It thus appears that the plan itself, later effectuated by the action of the security holders, contemplated not only that the new road would be operated by the Big

Four but that the Big Four was at the outset, to own at least one-half of the common stock of the new railroad. Thus the O. W. & I. shareholders, who by exchange became P. & E. shareholders, knew that the Big Four was to have both a stock interest and at the same time a contract to operate the road.

This basic intention and consideration is plainly stated in the contract between the Coster Committee and the Big Four, dated October 30, 1889, of which, as we have said, the Re-organization Plan was a part (S. 156-9).

Thus the contract shows that at the very inception of the relationship it was intended by the Big Four that it would not buy the Eastern line or operate the Western line under a separate corporate form, unless it had one-half stock ownership in the new Western company. The contract provided in part:

> "* * * when the Committee shall have so far carried out the said reorganization as that the said Western line and the said Eastern line shall have become or can be separated, then upon transfer and delivery to it of one-half of the stock of the Company owning said Western line issued under said reorganization, it will purchase or otherwise take over the said Eastern line, subject to and charged with a purchase money lien on the property only amounting to five million dollars. * * *" (S. 156, 7)

and also declared that the Big Four

> "* * * will also simultaneously enter into a lease or other operating contract whereby it shall undertake the operation and management of said Western line and agree (1) that the net earnings of said Western line shall be applied likewise to

> the payment of the interest to accrue on the said prior bonds, also on one million dollars other prior bonds having a lien on the Western line only, and on said new First Consolidated Mortgage Bonds, and (2) that the balance of such net earnings from the Western line and income derived from the lien on the Eastern line shall after payment of said interest be paid over to the Western Company" (S. 157).

At the same time the intention of the parties with respect to the operation of the Western Company (the P. & E.) was defined by stating that the contract:

> "* * * shall also contain covenants whereby said Cleveland Co. shall undertake to maintain said Western line and the rolling stock necessary for the operation of said Western line, and pay all taxes thereon or upon the earnings or income of said Western line as well as rentals or other like charges, and to indemnify and save harmless said Western Company from all claims arising out of the operation or management thereof, and also such other covenants, terms and conditions as may be reasonably required by said Committee, pursuant to the plan of reorganization, or for the more perfect protection of the holders of said prior bonds and said new First Consolidated Mortgage Bonds and new income bonds and stock to be issued under said plan of reorganization, and the rights and interests intended to be granted to them" (S. 158).

The arrangements contemplated by the plan and the contract were effected in 1890. At that time the mortgages were executed, the new bonds, including the Income Bonds, were issued, the Big Four bought the Springfield division outright, received a one-half

common stock interest in the new Western Company (the P. & E.), and entered into the operating agreement (S. 160-171) with it on February 21, 1890.

The transaction, viewed as a whole, indicates that the Big Four, then operating connecting and related lines in the same territory, would operate the P. & E. for the mutual advantage of the two roads, and indeed, the operating agreement recited:

> "Whereas, the railways of the parties hereto connect at Indianapolis, and it will be beneficial to the business and traffic of said railways that the same be put under one management: * * *" (S. 162).

The operating agreement comprehends the following rights and obligations:

> (1) The Big Four received the right to "use" the P. & E., subject to the other terms of the agreement.
>
> (2) The Big Four agreed that for 50 years beginning on April 1, 1890, it would operate and use the road in accordance with law, providing at its own cost all rolling stock and equipment, labor and supplies, and that it would maintain the road, and its rolling stock, pay all taxes, and indemnify the P. & E. from all claims arising out of management.
>
> (3) The Big Four agreed to pay the interest on the First Mortgage consolidated bonds.
>
> (4) The Big Four was to receive all net income, and after paying the senior fixed and other charges and expenses of operation, agreed to pay the balance of the net earnings, in any year, after recoupment of all advances (1) on the interest

due to the Income Bonds and (2) the remaining balance, if any, to the P. & E.

(5) The Big Four agreed to render proper accounts of earnings and disbursements to the P. & E. and the trustees of the Second Income Mortgage, within 60 days after December 31, of each year.

(6) The Big Four agreed to look only to such future net earnings as were not required for payment of fixed charges, for reimbursement of sums advanced under the agreement and the P. & E. agreed to charge all such earnings for that purpose, such advances to carry interest at 6%.

(7) The P. & E. agreed to let the Big Four use its name.

(8) The P. & E. had the right to resume operations in the event of default by the Big Four and in that event, or at the termination of the agreement, the Big Four agreed to return all rolling stock, etc. or its equivalent.

On the same day the operating agreement was executed between the Big Four and the P. & E., Income Bonds were created by indenture, as provided in the Plan of Reorganization (S. 178-201; Exs. 3, 13). This document recited the intention of the P. & E. to issue $4,000,000 of bonds "with interest thereon at a rate not exceeding four percent in any one year, payable * * * only out of the net earnings and income of the Railway Company as the same shall be ascertained for each particular year * * * such interest to be absolutely non-cumulative" (S. 179). The mortgage was not only subordinate to prior liens but to the operating agreement.

It was provided that the Board of Directors should ascertain and declare the net earnings after all charges and after reimbursement of all advances of the road by December 31st of each year, and pay the interest due by April 1st of each year. The Railway Company was required to furnish the trustee with a statement of earnings each year and it was provided that the trustee, on its own motion, or after notification by 20% of the bondholders, should, if dissatisfied, notify the Railway Company of such objection. If no adjustment was made the trustee, if called upon so to do by 20% of the bondholders, was authorized and directed to sue for an accounting. This procedure and this remedy were exclusive of all others (S. 192-5).

Also in conformity with the reorganization plan the Big Four, simultaneously with the execution of the operating agreement, acquired 50% of the common stock of the P. & E. At about the same time it acquired for cash one additional share of that stock, thus achieving complete voting control (Findings of Fact 16, 17, 18, S. 119-120).

Thus, at this stage in the history of this relationship we find the Big Four, presumably a solvent road operating in adjacent territory and connecting with the old O. W. & I., taking that line over by purchasing the Eastern half and by agreeing to operate the Western half, transformed into a new company, on a mutual benefit basis, including as an express condition of the transaction, ownership of at least one-half of the equity and voting power represented by the common stock.

The P. & E. from the outset, under these arrangements, has never operated its properties, nor was it ever intended to. On the contrary, it seems clear that it was the express intention and desire of all of

the parties, including the share owners and bondholders of the P. & E., that, however the legal relationship might be defined, the Big Four was to operate the road as part of a system supplying, both capital and management, and having only the duty to pay over or account for the net income on the terms specified in the contract. For this assumption of the obligation of management and of financing the venture, the Big Four received the right to operate the line as part of its own system.

There was no change in these basic agreements and arrangements until January 2, 1930, when the Big Four leased to the New York Central Railroad all its line of railroad and other property, including a transfer of its rights under the operating agreement (Finding of Fact No. 19; S. 120; Ex. 15). Since that time the Central has succeeded to the rights and responsibilities of the Big Four under the arrangements made in 1890, including the operating agreement.

As already noted, the District Court by its decree in the adjustment proceeding continued the operating agreement in effect for an additional term of twenty years (S. 106; 134-151; 172-177).

From the foregoing history of the Peoria company the following facts have particular significance in determining the legal relations between the parties.

The Big Four, in 1889, agreed to purchase one-half of the O. W. & I. and to operate the other, providing it received, among other things, one-half of the common stock of the new company, the P. & E., and the right to use the lines of the P. & E., presumably as part of its system.

It is thus clear that the security holders of the O. W. & I., who became the security holders of the P. & E., bargained at the outset not for merely an operating agent, but for an operating agent which would be a half owner in the business. The security holders knew, too, that the operating agent was a connecting, and in some directions, a competing carrier. Notwithstanding this they consented to a plan of reorganization which contemplated management of their road by such a competing carrier.

We come then to the operating agreement. This plainly, and in light of the circumstances surrounding and preceding its execution, did not create any express trust. It was an arrangement based on the fact, as it recited, that it would be mutually beneficial for these connecting carriers to be operated under one management. It was a bargain, dictated by neither party, whereby each gave and each received. The P. & E. received guarantees of payment of its fixed indebtedness; guarantees of maintenance and operation at the sole expense of the Big Four, including indemnity against deficits and finally the right to any net earnings after deduction of all expenses, advances and fixed charges.

On its side, the Big Four received the right to use the road, with which it connected, during the term of the agreement. This was, presumably, a valuable right, and one for which the Big Four was willing to make the commitments set forth in the agreement.

At this point, without considering the effect of further voting control, it seems clear that the Big Four had bargained for and obtained absolute control over the operations of the P. & E. during the term of the agreement. By its bargain, and as the result of the very nature of the arrangement, it had

both the right and the duty to make every decision affecting the operation and maintenance of the P. & E. Further, it was plain from the very nature of the relationship that the decisions made by the Big Four with respect to the P. & E. would affect not only the P. & E. but its own lines. The arrangement could not have existed otherwise.

We believe, therefore, that at least insofar as the operating agreement governed the relationship of the parties it imposed no extraordinary fiduciary obligation upon the operating companies. The question next arises, however, as to the extent, if any, to which domination by the operating companies through stock control created a fiduciary relationship out of which a higher duty arose.

We suggest that, in view of the circumstances and conditions surrounding the execution and performance of the operating agreement, no clear fiduciary duty existed between the parties with respect to matters arising under the operating contract. Clearly the fact of domination and control created no express trust since such a trustee may deal itself with the property of a beneficiary only at its peril. The arrangement here not only contemplated but required that the Operating Companies deal in a multitude of vital matters affecting important property rights as well as the day to day business of the parties. This clearly negatives the trust conception applied in the cases cited by the petitioners.

Even if it is concluded that, by reason of domination and control, a fiduciary relationship exists, the mere statement of that fact does not solve the problem. As this Court observed in *S. E. C.* v. *Chenery Corporation,* 318 U. S. 80, 85-6: "* * * to say that a man is a fiduciary only begins analysis; it gives direction

to further inquiry. * * * What obligations does he owe as a fiduciary? In what respect has he failed to discharge these obligations? And what are the consequences of his deviation from duty?"

If there were no operating agreement the case would be merely one of domination and control of a parent by a subsidiary giving rise to a strictly enforceable fiduciary duty (*Geddes* v. *Anaconda Copper Mining Co.*, 254 U. S. 590 (1921); *Chelrob, Inc.* v. *Barrett*, 293 N. Y. 442 (1944)). However, this is not a situation where the parent was free to deal with a subsidiary or not, as it saw fit, and where in consequence it could be required to deal only as a fiduciary. Here the underlying and basic circumstances contemplated by the parties at the outset required the parent to deal with the subsidiary, and, moreover, required the parent by almost every decision it made to make a decision which not only affected the subsidiary but also affected itself. In such a situation the fiduciary obligation is clearly affected and limited by the contractual obligations between the parties (*Blaustein* v. *Pan Am. etc.*, 293 N. Y. 281).

The suggestion in such cases as *Chelrob* v. *Barrett*, *supra*, that the sole test of the propriety of the parent's conduct is whether it is fair to the subsidiary would, in these circumstances seem inapplicable to all transactions which came clearly within the scope of the operating agreement. In such cases, it would seem that the intention of the parties, the requirements of the underlying situation and the terms of the agreement require that in considering any given transaction between the operating companies and the P. & E., effect be given to all these considerations and

that an effort be made to ascertain the fairness of the transaction in the light of its effect upon both parties.

An examination of the cases cited by the petitioners indicates that where a fiduciary duty has been declared there has been either fraud (and there is no suggestion of fraud on this record) or direct damage to the property of a subsidiary by a parent, or of the property of a minority by a majority interest. None of the authorities so holding involve a situation, as here, where the underlying contractual relations between the parties required operation of all of the business of one by the other.

It is, therefore, our view that the relationship of the parties, considered in the light of its inception and in the light of the requirements of the P. & E., does not involve any fiduciary duty but involves only a contractual relationship based on a mutual benefit. It is our view, too, that any other construction of the agreement would be necessarily detrimental to the best interests of the P. & E. on the whole, since if a strict fiduciary relationship existed here the Operating Companies would not and could not operate the P. & E. on a basis which would justify the continuance of the P. & E. As we have previously indicated, the relationship between the parties did not involve the fiduciary obligations contended for by the Income Bondholders. Indeed, to apply the principle to the special contractual situation existing here would, as the District Court pointed out, require that "after the lapse of fifty years, the contract should be unravelled." (*Ewen* v. *Peoria and Eastern Railway Co.*, 34 F. Supp. 332, 335.)

II.

It is suggested by the Income Bondholders that the District Court was also in error as to burden of proof; in holding, unnecessarily, that the Income Bondholders were bound by the terms of their mortgage, and that the ten-year New York State Statute of Limitations should not have been applied (Petition, pp. 30-40).

In making these contentions we believe that the Income Bondholders have lost sight of the fact that the statement of these accounts is only a part of the effectuation of a plan of adjustment which must, under Section 710(2)(c)(ii) of the Bankruptcy Act (53 Stat. 1134), be "in the public interest and in the best interests of each class of creditors and stockholders".

The hearings before the Special Master consumed many weeks. More than 4,000 pages of testimony were taken and hundreds of exhibits were introduced by the parties. Every issue which could conceivably be raised was exhaustively investigated on the record and all the evidence which could possibly be assembled by any of the parties was laid before the Court. The Special Master in a 300-page report analyzed all of the evidence on every issue. The Court, with a minor exception, which made no difference to the P. & E., confirmed the Master's report, after a full presentation of the issues by counsel orally and in voluminous briefs.

All of this resulted in enormous expense which was borne by the P. & E. and which far exceeded the comparatively small amount of adjustments made in the accounts.

In this connection, we respectfully point out that as a result of the proceedings by the Income Bondholders, the P. & E. received adjustments in its favor of only $176,260.36, including interest (S. 8). At the same time, due to the fact that the sum of $1,579,162.32, representing its net earnings for 1942, 1943 and 1944 was held in a special account, and not applied in reduction of advances made by the Operating Companies, the P. & E. was deprived of interest on that sum (S. 77-78). This amounted to $342,637.47. The P. & E. has thus lost, as a result of these proceedings, taken at the instance of one class of creditors, the sum of $166,377.11, being the difference between the adjustments of $176,260.36 and $342,637.47, without even considering the other expenses of the proceeding.

We, therefore, suggest that the phase of the adjustment proceedings which the Income Bondholders seek to have this Court review has not been "in the public interest and in the best interests of each class of creditors and stockholders", as required by the Act (53 Stat. 1134). We suggest, also, that a further examination of the evidence could only result in additional heavy expense to the P. & E., without any substantial likelihood of any improvement in the plan of adjustment or of financial benefit to the P. & E., as a whole.

Respectfully submitted,

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